

AMENDED IN SENATE MAY 14, 2007

AMENDED IN SENATE APRIL 9, 2007

**SENATE BILL**

**No. 359**

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**Introduced by Senators Runner and Dutton**

February 20, 2007

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An act to amend Sections 17052.12 and 23609 of, to amend, add, and repeal Section 25128 of, and to add and repeal Sections 6357.7, 6377, 6902.5, 17053.36, 17053.37, 17053.85, 17053.86, 23636, 23637, 23685, and 23686 of, 23609, and 25128 of, and to add and repeal Section 6357.7 of, the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

LEGISLATIVE COUNSEL'S DIGEST

SB 359, as amended, Runner. Sales and use taxes: exemptions: income and corporation taxes: credits: ~~qualified motion picture production.~~ *corporation tax allocations.*

(1) The Sales and Use Tax Law imposes a tax on the gross receipts from the sale in this state of, or the storage, use, or other consumption in this state of, tangible personal property. That law provides various exemptions from that tax, including an exemption for the gross receipts from the sale of, and the storage, use, or other consumption of, fuel and petroleum products sold to an air common carrier for immediate consumption or shipment in the conduct of its business on an international flight.

This bill would, from January 1, 2008, until an December 31, 2017, exempt from those state taxes gross receipts in excess of ~~\$1.88~~ \$1.66 per gallon derived from the sale in this state of, and the storage, use, or other consumption in this state of, fuel and petroleum products sold to or purchased by an air common carrier on a domestic flight, as specified.

~~(2) The Sales and Use Tax Law imposes a tax on the gross receipts from the sale in this state of, or the storage, use, or other consumption in this state of, tangible personal property and provides various exemptions from the taxes imposed by that law.~~

~~This bill would, for calendar years beginning on or after January 1, 2008, and before January 1, 2018, allow an exemption from those taxes for the gross receipts from the sale of, and the storage, use, or other consumption of, tangible personal property, as defined, purchased for use by a qualified person, as defined, engaged in the manufacturing, processing, refining, fabricating, or recycling of property, as specified.~~

~~(3) The Personal Income Tax Law and the Corporation Tax Law authorize various credits against the taxes imposed by those laws.~~

~~This bill would authorize a credit against those taxes, until January 1, 2017, for taxable years beginning on or after January 1, 2007, subject to specified limitations, in an amount equal to 12% of the qualified amount for qualified wages paid or incurred with respect to the production of each qualified motion picture with an additional 3% for specific qualified motion pictures.~~

~~Additionally, this bill would authorize a credit against those taxes, until January 1, 2017, for taxable years beginning on or after January 1, 2007, subject to specified limitations, in an amount equal to 10% of the incremental qualified production costs paid or incurred with respect to the production of qualified commercials, as defined.~~

~~This bill would, in lieu of the credits authorized under the Personal Income Tax and Corporation Tax Law for qualified motion pictures allow a credit against liability for taxes paid or payable, as applicable, under the Sales and Use Tax Law for qualified motion pictures. This bill would impose specified duties on the California Film Commission and the Franchise Tax Board in administering the credits.~~

~~This bill would require the Business, Transportation and Housing Agency to report to the Legislature regarding the effectiveness of the tax incentives created by the bill.~~

~~The bill would require a taxpayer to certify under penalty of perjury that he or she is the taxpayer entitled to claim certain deductions with respect to a qualified motion picture, thus imposing a state-mandated local program by expanding the scope of an existing crime.~~

~~The California Constitution requires the state to reimburse local agencies and school districts for certain costs mandated by the state. Statutory provisions establish procedures for making that reimbursement.~~

~~This bill would provide that no reimbursement is required by this act for a specified reason:~~

~~(4)~~

(2) The Personal Income Tax Law and the Corporation Tax Law, by reference to a specified federal statute, allow a credit against taxes imposed by those laws for increasing research expenses, as defined. In general, the amount of the credit under both laws is equal to 15% of the excess of the qualified research expenses, as defined, for the taxable year over the base amount, as defined, and, in addition, for purposes of the Corporation Tax Law, 24% of the basic research payments, as defined. The term “base amount” means the product of the average annual gross receipts of the taxpayer for each of the specified years preceding the taxable year and the fixed-base percentage, as defined, but in no event less than 50% of the qualified research expenses for the taxable year. A taxpayer may elect an alternative incremental credit for increasing research expenses in modified conformity to federal income tax laws.

This bill would modify the credit for increasing research expenses to 16% of the excess of the qualified research expenses. This bill would also make modification to alternative incremental credit provided under those federal income tax laws.

~~(5) The Personal Income Tax Law and the Corporation Tax Law authorize various credits against the taxes imposed by those laws:~~

~~This bill would, for taxable years beginning on or after January 1, 2007, and before January 1, 2017, authorize a credit against those taxes for specified taxable years, in an amount equal to a specified percentage of the qualified wages, as defined, paid, or incurred during the taxable or income year or in connection with an initial contract or subcontract to manufacture property for ultimate use in a Joint Strike Fighter or Crew Exploration Vehicle, as defined. This bill would also authorize, for taxable years beginning on or after January 1, 2007, and before January 1, 2017, a credit in an amount equal to 10% of the qualified cost, as provided, of property for use in the manufacture of a product for ultimate use in a Joint Strike Fighter or Crew Exploration Vehicle, as defined.~~

~~(6) The Corporation Tax Law imposes taxes measured by income and, in the case of a business with income derived from or attributable to sources both within and without this state, apportions the income between this state and other states and foreign countries in accordance with a specified 4-factor formula based on the property, payroll, and~~

~~sales within and without this state, except that in the case of an apportioning trade or business that derives more than 50% of its gross business receipts from conducting one or more qualified business activities, as defined, including an extractive business activity, business income is apportioned in accordance with a specified 3-factor formula.~~

~~This bill would permit, by election, business income of a qualified taxpayer, as defined, to be apportioned to this state, for taxable years beginning on or after January 1, 2007, and before January 1, 2017, by multiplying the business income by a fraction, the numerator of which is the property factor plus the payroll factor plus 4 times the sales factor, and the denominator of which is 6.~~

~~This bill would also provide that, for taxable years beginning on or after January 1, 2007, and before January 1, 2017, a taxpayer that is neither a qualified taxpayer nor engaged in a specified business activity must apportion its business income to this state in accordance with the 4-factor formula, and would specify that, with respect to a certain business activity, a trade or business would be allowed to apportion its business income based upon the revised formula or in accordance with the 3-factor formula, as provided, and would specify that, with respect to certain qualified business activities, a trade or business must apportion its business income to this state in accordance with the 3-factor formula.~~

~~This bill, for purposes of the sales factor, would provide that notwithstanding the Multistate Tax Compact, gross receipts would also define the term “total sales arising from a treasury function,” as defined, to mean only the overall net gain, including interest and dividends, realized by the taxpayer from transactions undertaken as part of its treasury function, as defined.~~

~~(3) *The Corporation Tax Law imposes taxes measured by income and, in the case of a business with income derived from, or attributable to, sources both within and without this state, apportions the income between this state and other states and foreign countries in accordance with a specified 4-factor formula, except as otherwise provided.*~~

~~This bill, for taxable years beginning on or after January 1, 2007, would allow a taxpayer that is a member of the apportioning trade or business to elect, by contracting with the Franchise Tax Board, as provided, to apportion its business income to this state by utilizing one of the revised apportionment formulas, as specified.~~

~~(7)~~

~~(4) Counties and cities are authorized to impose local sales and use taxes in conformity with state sales and use taxes. Exemptions from~~

state sales and use taxes enacted by the Legislature are automatically incorporated into the local taxes.

This bill would specify that this exemption does not apply to local sales or transactions and use taxes, unless the governing body of the taxing county, city, or district votes otherwise.

~~(8)~~

(5) This bill would take effect immediately as a tax levy.

Vote: majority. Appropriation: no. Fiscal committee: yes.

State-mandated local program: ~~yes~~ no.

*The people of the State of California do enact as follows:*

1 SECTION 1. Section 6357.7 is added to the Revenue and  
2 Taxation Code, to read:

3 6357.7. (a) From January 1, 2008, to December 31, 2017,  
4 inclusive, there are exempted from the taxes imposed by this part,  
5 those gross receipts in excess of one dollar ~~eighty-eight cents~~  
6 ~~(\$1.88)~~ *sixty-six cents (\$1.66)* per gallon derived from the sale in  
7 this state of, or the storage, use, or other consumption in this state  
8 of, fuel and petroleum products sold to or purchased by an air  
9 common carrier for consumption or shipment in the conduct of its  
10 business as an air common carrier, on a domestic flight.

11 (b) To qualify for the exemption, the air common carrier shall  
12 furnish to the seller an exemption certificate in the form prescribed  
13 by the board. Acceptance in good faith of that certificate shall  
14 relieve the seller from liability for the sales tax exempted under  
15 this section.

16 (c) For purposes of this section, the following definitions apply:

17 (1) "Air common carrier" has the same meaning as that set forth  
18 in Section 23046 of the Business and Professions Code.

19 (2) "Domestic flight" means a flight whose final destination is  
20 a point inside of the United States, including its territories.

21 (d) Any air common carrier claiming exemption under this  
22 section, who is not required to hold a valid seller's permit, shall  
23 be required to register with the board and obtain a fuel exemption  
24 registration number, and shall be required to file returns as the  
25 board may prescribe, either if the board notifies the carrier that  
26 returns must be filed or if the carrier is liable for taxes based upon  
27 consumption or transportation of fuel or petroleum products  
28 erroneously claimed as exempt under this section.

(e) An air common carrier claiming an exemption under this section, upon request, shall make available to the board records, including, but not limited to, a copy of a log abstract, an air waybill, or a cargo manifest, documenting its consumption or transportation of the fuel or petroleum products on a domestic flight and the amount claimed as exempt. If the carrier fails to provide these records upon request, the board may revoke the carrier's fuel exemption registration number.

(f) The board may require any air common carrier claiming an exemption under this section and required to obtain a fuel exemption registration number, to place with it such security as the board may determine pursuant to Section 6701.

(g) Pursuant to this section, any use of the fuel and petroleum products by the purchasing carrier, other than that incident to the delivery of the fuel and petroleum products to the carrier and the consumption or transportation of the fuel and petroleum products by the carrier on a domestic flight for use in the conduct of its business as a common carrier, or a failure of the carrier to document its consumption or transportation of the fuel and petroleum products on a domestic flight, shall subject the carrier to liability for payment of sales tax as if it were a retailer making a retail sale of the property at the time of that use or failure, and the sales price of the property to it shall be deemed to be the gross receipts from the retail sale.

(h) Notwithstanding any provision of the Bradley-Burns Uniform Local Sales and Use Tax Law (Part 1.5 (commencing with Section 7200)) or the Transactions and Use Tax Law (Part 1.6 (commencing with Section 7251)), the exemption established by this section shall not apply with respect to any tax levied by a county, city, or district pursuant to, or in accordance with, either of those laws, unless approved by the local government that would otherwise receive the revenues derived from the taxes imposed under those laws.

(i) This section shall remain in effect only until January 1, 2018, and as of that date is repealed.

~~SEC. 2. Section 6377 is added to the Revenue and Taxation Code, to read:~~

~~6377. (a) For calendar years beginning on or after January 1, 2008, there are exempted from the taxes imposed by this part the~~

gross receipts from the sale of, and the storage, use, or other consumption in this state of, any of the following:

(1) Tangible personal property purchased for use by a qualified person to be used primarily in any stage of the manufacturing, processing, refining, fabricating, or recycling of property, beginning at the point any raw materials are received by the qualified person and introduced into the process and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling has altered property to its completed form, including packaging, if required.

(2) Tangible personal property purchased for use by a qualified person to be used primarily in research and development.

(3) Tangible personal property purchased for use by a qualified person to be used primarily to maintain, repair, measure, or test any property described in paragraph (1), (2), or (3).

(4) Tangible personal property purchased for use by a contractor purchasing that property either as an agent of a qualified person or for the contractor's own account and subsequent resale to a qualified person for use in the performance of a construction contract for the qualified person who will use the tangible personal property as an integral part of the manufacturing, processing, refining, fabricating, or recycling process, or as a research or storage facility for use in connection with the manufacturing process.

(b) This exemption does not apply to any tangible personal property that is used primarily in administration, general management, or marketing.

(c) For purposes of this section:

(1) "Fabricating" means to make, build, create, produce, or assemble components or property to work in a new or different manner.

(2) "Manufacturing" means the activity of converting or conditioning property by changing the form, composition, quality, or character of the property for ultimate sale at retail or use in the manufacturing of a product to be ultimately sold at retail. Manufacturing includes any improvements to tangible personal property that result in a greater service life or greater functionality than that of the original property.

(3) "Primarily" means tangible personal property used 50 percent or more of the time in an activity described in subdivision (a).

~~(4) (A) “Process” means the period beginning at the point at which any raw materials are received by the qualified taxpayer and introduced into the manufacturing, processing, refining, fabricating, or recycling activity of the qualified taxpayer and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling activity of the qualified taxpayer has altered tangible personal property to its completed form, including packaging, if required. Raw materials shall be considered to have been introduced into the process when the raw materials are stored on the same premises where the qualified taxpayer’s manufacturing, processing, refining, fabricating, or recycling activity is conducted.~~

~~(B) Raw materials that are stored on premises other than where the qualified taxpayer’s manufacturing, processing, refining, fabricating, or recycling activity is conducted, shall not be considered to have been introduced into the manufacturing, processing, refining, fabricating, or recycling process.~~

~~(5) “Processing” means the physical application of the materials and labor necessary to modify or change the characteristics of property.~~

~~(6) “Qualified person” means any person that is both of the following:~~

~~(A) A new trade or business. In determining whether a trade or business activity qualifies as a new trade or business, the following rules shall apply:~~

~~(i) In any case where a person purchases or otherwise acquires all or any portion of the assets of an existing trade or business, irrespective of the form of entity, that is doing business in this state, within the meaning of Section 23101, the trade or business thereafter conducted by that person or any related person shall not be treated as a new business if the aggregate fair market value of the acquired assets, including, real, personal, tangible, and intangible property, used by that person or any related person in the conduct of his or her trade or business exceeds 20 percent of the aggregate fair market value of the total assets of the trade or business being conducted by the person or any related person. For purposes of this subparagraph only, the following rules shall apply:~~

~~(I) The determination of the relative fair market values of the acquired assets and the total assets shall be made as of the last day of the month following the quarterly period in which the person~~



1 or any related person first uses any of the acquired trade or business  
2 assets in his or her business activity.

3 (II) ~~Any acquired assets that constituted property described in~~  
4 ~~Section 1221(1) of the Internal Revenue Code in the hands of the~~  
5 ~~transferor shall not be treated as assets acquired from an existing~~  
6 ~~trade or business, unless those assets also constitute property~~  
7 ~~described in Section 1221(1) of the Internal Revenue Code in the~~  
8 ~~hands of the acquiring person or related person.~~

9 (ii) ~~In any case where a person or any related person is engaged~~  
10 ~~in one or more trade or business activities in this state, or has been~~  
11 ~~engaged in one or more trade or business activities in this state~~  
12 ~~within the preceding 36 months (“prior trade or business activity”),~~  
13 ~~and thereafter commences an additional trade or business activity~~  
14 ~~in this state, the additional trade or business activity shall only be~~  
15 ~~treated as a new business if the additional trade or business activity~~  
16 ~~is classified under a different division of the Standard Industrial~~  
17 ~~Classification Manual published by the United States Office of~~  
18 ~~Management and Budget, 1987 edition, than are any of the person’s~~  
19 ~~or any related person’s current or prior trade or business activities~~  
20 ~~in this state.~~

21 (iii) ~~In any case where a person, including all related persons,~~  
22 ~~is engaged in trade or business activities wholly outside of this~~  
23 ~~state and that person first commences doing business in this state,~~  
24 ~~within the meaning of Section 23101, after December 31, 2002,~~  
25 ~~other than by purchase or other acquisition described in clause (i);~~  
26 ~~the trade or business activity shall be treated as a new business.~~

27 (iv) ~~In any case where the legal form under which a trade or~~  
28 ~~business activity is being conducted is changed, the change in form~~  
29 ~~shall be disregarded and the determination of whether the trade or~~  
30 ~~business activity is a new business shall be made by treating the~~  
31 ~~person as having purchased or otherwise acquired all or any portion~~  
32 ~~of the assets of an existing trade or business under the rules of~~  
33 ~~clause (i).~~

34 (v) ~~“Related person” means any person that is related to that~~  
35 ~~person under either Section 267 or 318 of the Internal Revenue~~  
36 ~~Code.~~

37 (vi) ~~“Acquire” includes any gift, inheritance, transfer incident~~  
38 ~~to divorce, or any other transfer, whether or not for consideration.~~

39 (B) ~~Engaged in those lines of business described in Codes 2011~~  
40 ~~to 3999, inclusive, and Codes 7371 to 7373, inclusive, of the~~

1 Standard Industrial Classification Manual published by the United  
2 States Office of Management and Budget, 1987 edition, or engaged  
3 in telecommunication activities.

4 (7) Notwithstanding paragraph (6), “qualified person” shall not  
5 include any person who has conducted business activities in a new  
6 trade or business for three or more years.

7 (8) “Recycling” means using, reusing, or reclaiming a recyclable  
8 material to produce new or recycled property.

9 (9) “Refining” means the process of converting a natural  
10 resource to an intermediate or finished product.

11 (10) “Research and development” means those activities that  
12 are described in Section 174 of the Internal Revenue Code or in  
13 any regulations promulgated under that section.

14 (11) “Tangible personal property” does not include any of the  
15 following:

16 (A) Consumables with a normal useful life of less than one year,  
17 except as provided in subparagraph (E) of paragraph (11):

18 (B) Furniture, inventory, equipment used in the extraction  
19 process, or equipment used to store finished products that have  
20 completed the manufacturing process:

21 (12) “Tangible personal property” includes, but is not limited  
22 to, all of the following:

23 (A) Machinery and equipment, including component parts and  
24 contrivances such as belts, shafts, moving parts, and operating  
25 structures:

26 (B) All equipment or devices used or required to operate,  
27 control, regulate, or maintain the machinery, including, without  
28 limitation, computers, data processing equipment, and computer  
29 software, together with all repair and replacement parts with a  
30 useful life of one or more years, whether purchased separately or  
31 in conjunction with a complete machine and regardless of whether  
32 the machine or component parts are assembled by the taxpayer or  
33 another party:

34 (C) Property used in pollution control that meets or exceeds  
35 standards established by this state or any local or regional  
36 governmental agency within this state.

37 (D) Special purpose buildings and foundations used as an  
38 integral part of the manufacturing, processing, refining, or  
39 fabricating process, or that constitute a research or storage facility  
40 used during the manufacturing process. Buildings used solely for

1 ~~warehousing purposes after completion of the manufacturing~~  
2 ~~process are not included.~~

3 ~~(E) Fuels used or consumed in the manufacturing process.~~

4 ~~(F) Property used in recycling.~~

5 ~~(d) No exemption is allowed under this section unless the~~  
6 ~~purchaser furnishes the retailer with an exemption certificate,~~  
7 ~~completed in accordance with any instructions or regulations as~~  
8 ~~the board may prescribe, and the retailer subsequently furnishes~~  
9 ~~the board with a copy of the exemption certificate. The exemption~~  
10 ~~certificate shall contain the sales price of the machinery or~~  
11 ~~equipment that is exempt pursuant to subdivision (a).~~

12 ~~(e) Notwithstanding any provision of the Bradley-Burns Uniform~~  
13 ~~Local Sales and Use Tax Law (Part 1.5 (commencing with Section~~  
14 ~~7200)) or the Transactions and Use Tax Law (Part 1.6~~  
15 ~~(commencing with Section 7251)), the exemption established by~~  
16 ~~this section does not apply with respect to any tax levied by a~~  
17 ~~county, city, or district pursuant to, or in accordance with, either~~  
18 ~~of those laws.~~

19 ~~(f) (1) Notwithstanding subdivision (a), the exemption provided~~  
20 ~~by this section does not apply to any sale or use of property which,~~  
21 ~~within one year from the date of purchase, is either removed from~~  
22 ~~California or converted from an exempt use under subdivision (a)~~  
23 ~~to some other use not qualifying for the exemption.~~

24 ~~(2) The exemption established by this section does not apply~~  
25 ~~with respect to any tax levied pursuant to Sections 6051.2 and~~  
26 ~~6201.2, or pursuant to Section 35 of Article XIII of the California~~  
27 ~~Constitution.~~

28 ~~(g) If a purchaser certifies in writing to the seller that the~~  
29 ~~property purchased without payment of the tax will be used in a~~  
30 ~~manner entitling the seller to regard the gross receipts from the~~  
31 ~~sale as exempt from the sales tax, and within one year from the~~  
32 ~~date of purchase, the purchaser (1) removes that property outside~~  
33 ~~California, (2) converts that property for use in a manner not~~  
34 ~~qualifying for the exemption, or (3) uses that property in a manner~~  
35 ~~not qualifying for the exemption, the purchaser shall be liable for~~  
36 ~~payment of sales tax, with applicable interest, as if the purchaser~~  
37 ~~were a retailer making a retail sale of the property at the time the~~  
38 ~~property is so removed, converted, or used, and the sales price of~~  
39 ~~the property to the purchaser shall be deemed the gross receipts~~  
40 ~~from that retail sale.~~

~~(h) This section applies to leases of tangible personal property classified as “continuing sales” and “continuing purchases” in accordance with Sections 6006.1 and 6010.1. The exemption established by this section applies to the rentals payable pursuant to a lease, provided the lessee is a qualified person and the property is used in an activity described in subdivision (a). Rentals that meet the foregoing requirements are eligible for the exemption for a period of six years from the date of commencement of the lease. At the close of the six-year period from the date of commencement of the lease, lease receipts are subject to tax without exemption.~~

~~(i) This section shall remain in effect only until January 1, 2018, and as of that date is repealed.~~

~~SEC. 3.— Section 6902.5 is added to the Revenue and Taxation Code, to read:~~

~~6902.5. (a) A qualified taxpayer, as designated by the California Film Commission pursuant to subdivision (h) of Section 17053.85 or 23685, that makes an irrevocable election pursuant to subdivision (h) of Section 17053.85 or 23685 to claim the credit authorized by this section, may claim that credit as either a refund of sales or use taxes paid under this part, or a credit against liability for sales or use taxes due under this part, that is equal to the credit amount that would otherwise be allowed pursuant to those sections.~~

~~(b) Notwithstanding Section 6961, the board may recover any refund or credit, or part thereof, that is erroneously made pursuant to this section. In recovering any erroneous refund or credit made pursuant to this section, the board, in its discretion, may issue a deficiency determination in accordance with Article 2 (commencing with Section 6481) of, or Article 4 (commencing with Section 6536) of, Chapter 5. Except in the case of fraud, that determination shall be made within three years from the last day of the month following the quarterly period in which the board approved the refund.~~

~~(c) In the case where the credit allowed by this section exceeds the qualified taxpayer’s tax liability computed under this part, the excess shall first be credited against other amounts due, if any, from the qualified taxpayer to this state, including, but not limited to, tax deficiencies, penalties, and interest assessed by the Franchise Tax Board, tax deficiencies, penalties, and interest assessed by the State Board of Equalization, child support payments, and payments due under the Unemployment Insurance Code, and the excess, if~~

1 any, may be carried over to reduce any amounts due to the  
2 Franchise Tax Board, the State Board of Equalization, or any  
3 payments due under the Unemployment Insurance Code in the  
4 following year, and succeeding years if necessary, until the credit  
5 is exhausted.

6 (d) ~~The board shall provide an annual listing to the Franchise~~  
7 ~~Tax Board, in a form and manner agreed upon by the board and~~  
8 ~~the Franchise Tax Board, of the qualified taxpayers who, during~~  
9 ~~the year, have claimed a refund or credit of sales or use tax under~~  
10 ~~this section and the amount of the refund or credit allowed to each~~  
11 ~~qualified taxpayer.~~

12 (e) ~~Section 6907, relating to interest on overpayments, shall not~~  
13 ~~apply to any return claiming a credit under this section.~~

14 (f) ~~The California Film Commission shall provide a list, at least~~  
15 ~~annually, to the State Board of Equalization, in the form and~~  
16 ~~manner as shall be determined by the California Film Commission~~  
17 ~~and the State Board of Equalization, of the names, taxpayer~~  
18 ~~identification numbers, including taxpayer identification numbers~~  
19 ~~of each partner or shareholder, as applicable, the qualified motion~~  
20 ~~pictures for which tax credit was allocated, and the total amount~~  
21 ~~of the tax credit allocated to each qualified taxpayer.~~

22 (g) ~~This section shall remain in effect only until January 1, 2018,~~  
23 ~~and as of that date is repealed, unless a later enacted statute, that~~  
24 ~~is enacted before January 1, 2018, deletes or extends that date.~~

25 ~~SEC. 4.~~

26 *SEC. 2.* Section 17052.12 of the Revenue and Taxation Code  
27 is amended to read:

28 17052.12. For each taxable year beginning on or after January  
29 1, 1987, there shall be allowed as a credit against the “net tax” (as  
30 defined by Section 17039) for the taxable year an amount  
31 determined in accordance with Section 41 of the Internal Revenue  
32 Code, except as follows:

33 (a) For each taxable year beginning before January 1, 1997, the  
34 reference to “20 percent” in Section 41(a)(1) of the Internal  
35 Revenue Code is modified to read “8 percent.”

36 (b) (1) For each taxable year beginning on or after January 1,  
37 1997, and before January 1, 1999, the reference to “20 percent”  
38 in Section 41(a)(1) of the Internal Revenue Code is modified to  
39 read “11 percent.”

(2) For each taxable year beginning on or after January 1, 1999, and before January 1, 2000, the reference to “20 percent” in Section 41(a)(1) of the Internal Revenue Code is modified to read “12 percent.”

(3) For each taxable year beginning on or after January 1, 2000, and before January 1, 2007, the reference to “20 percent” in Section 41(a)(1) of the Internal Revenue Code is modified to read “15 percent.”

(4) For each taxable year beginning on or after January 1, 2007, the reference to “20 percent” in Section 41(a)(1) of the ~~Internal Revenue Code~~ is modified to read “16 percent.” *Internal Revenue Code shall apply.*

(c) Section 41(a)(2) of the Internal Revenue Code, relating to basic research payments, shall not apply.

(d) “Qualified research” shall include only research conducted in California.

(e) In the case where the credit allowed under this section exceeds the “net tax,” the excess may be carried over to reduce the “net tax” in the following year, and succeeding years if necessary, until the credit has been exhausted.

(f) (1) With respect to any expense paid or incurred after the operative date of Section 6378, Section 41(b)(1) of the Internal Revenue Code is modified to exclude from the definition of “qualified research expense” any amount paid or incurred for tangible personal property that is eligible for the exemption from sales or use tax under Section 6378.

(2) For each taxable year beginning on or after January 1, 1998, the reference to “Section 501(a)” in Section 41(b)(3)(C) of the Internal Revenue Code, relating to contract research expenses, is modified to read “this part or Part 11 (commencing with Section 23001).”

(g) (1) For each taxable year beginning on or after January 1, 2000, and before January 1, 2007:

(A) The reference to “2.65 percent” in Section 41(c)(4)(A)(i) of the Internal Revenue Code is modified to read “one and forty-nine hundredths of one percent.”

(B) The reference to “3.2 percent” in Section 41(c)(4)(A)(ii) of the Internal Revenue Code is modified to read “one and ninety-eight hundredths of one percent.”

1 (C) The reference to “3.75 percent” in Section 41(c)(4)(A)(iii)  
2 of the Internal Revenue Code is modified to read “two and  
3 forty-eight hundredths of one percent.”

4 (2) ~~For each taxable year beginning on or after January 1, 2007,~~  
5 ~~the following apply:~~

6 (A) ~~The reference to “2.65 percent” in Section 41(c)(4)(A)(i)~~  
7 ~~of the Internal Revenue Code is modified to read “two percent.”~~

8 (B) ~~The reference to “3.2 percent” in Section 41(c)(4)(A)(ii) of~~  
9 ~~the Internal Revenue Code is modified to read “two and one-half~~  
10 ~~percent.”~~

11 (C) ~~The reference to “3.75 percent” in Section 41(c)(4)(A)(iii)~~  
12 ~~of the Internal Revenue Code is modified to read “three percent.”~~

13 (2) *For each taxable year beginning on or after January 1,*  
14 *2007, Section 41(c)(4) of the Internal Revenue Code, relating to*  
15 *the election of the alternative incremental credit, shall apply.*

16 (3) Section 41(c)(4)(B) shall not apply and in lieu thereof an  
17 election under Section 41(c)(4)(A) of the Internal Revenue Code  
18 may be made for any taxable year of the taxpayer beginning on or  
19 after January 1, 1998. That election shall apply to the taxable year  
20 for which made and all succeeding taxable years unless revoked  
21 with the consent of the Franchise Tax Board.

22 (4) Section 41(c)(6) of the Internal Revenue Code, relating to  
23 gross receipts, is modified to take into account only those gross  
24 receipts from the sale of property held primarily for sale to  
25 customers in the ordinary course of the taxpayer’s trade or business  
26 that is delivered or shipped to a purchaser within this state,  
27 regardless of f.o.b. point or any other condition of the sale.

28 (h) Section 41(h) of the Internal Revenue Code, relating to  
29 termination, shall not apply.

30 (i) Section 41(g) of the Internal Revenue Code, relating to  
31 special rule for passthrough of credit, is modified by each of the  
32 following:

33 (1) The last sentence shall not apply.

34 (2) If the amount determined under Section 41(a) of the Internal  
35 Revenue Code for any taxable year exceeds the limitation of  
36 Section 41(g) of the Internal Revenue Code, that amount may be  
37 carried over to other taxable years under the rules of subdivision  
38 (e); except that the limitation of Section 41(g) of the Internal  
39 Revenue Code shall be taken into account in each subsequent  
40 taxable year.

1 SEC. 5. ~~Section 17053.36 is added to the Revenue and Taxation~~  
2 ~~Code, to read:~~

3 ~~17053.36. (a) For each taxable year beginning on or after~~  
4 ~~January 1, 2007, and before January 1, 2017, a qualified taxpayer~~  
5 ~~shall be allowed as a credit against the “net tax,” as defined in~~  
6 ~~Section 17039, an amount equal to the following:~~

7 ~~(1) Fifty percent of qualified wages paid or incurred during any~~  
8 ~~taxable year beginning on or after January 1, 2007, and before~~  
9 ~~January 1, 2010.~~

10 ~~(2) Forty percent of qualified wages paid or incurred during any~~  
11 ~~taxable year beginning on or after January 1, 2010, and before~~  
12 ~~January 1, 2012.~~

13 ~~(3) Thirty percent of the qualified wages paid or incurred during~~  
14 ~~any taxable year beginning on or after January 1, 2012, and before~~  
15 ~~January 1, 2014.~~

16 ~~(4) Twenty percent of the qualified wages paid or incurred~~  
17 ~~during any taxable year beginning on or after January 1, 2014, and~~  
18 ~~before January 1, 2016.~~

19 ~~(5) Ten percent of the qualified wages paid or incurred during~~  
20 ~~any taxable year beginning on or after January 1, 2016, and before~~  
21 ~~January 1, 2017.~~

22 ~~(b) For purposes of this section:~~

23 ~~(1) (A) “Qualified taxpayer” means any taxpayer under an~~  
24 ~~initial contract or subcontract to manufacture property for ultimate~~  
25 ~~use in a Joint Strike Fighter or a Crew Exploration Vehicle.~~

26 ~~(B) In the case of any passthrough entity, the determination of~~  
27 ~~whether a taxpayer is a qualified taxpayer under this section shall~~  
28 ~~be made at the entity level and any credit under this section or~~  
29 ~~Section 23636 shall be allowed to the passthrough entity and passed~~  
30 ~~through to the partners or shareholders in accordance with~~  
31 ~~applicable provisions of this part or Part 11 (commencing with~~  
32 ~~Section 23001). For purposes of this paragraph, “passthrough~~  
33 ~~entity” means any partnership or “S” corporation.~~

34 ~~(2) “Qualified wages” means that portion of wages paid or~~  
35 ~~incurred by the qualified taxpayer during the taxable year with~~  
36 ~~respect to qualified employees that are direct costs as defined in~~  
37 ~~Section 263A of the Internal Revenue Code allocable to property~~  
38 ~~manufactured in this state by the qualified taxpayer for ultimate~~  
39 ~~use in a Joint Strike Fighter or a Crew Exploration Vehicle.~~



1     ~~(3) “Qualified employee” means an individual whose services~~  
2     ~~for the qualified taxpayer are performed in this state and are at~~  
3     ~~least 90 percent directly related to the qualified taxpayer’s contract~~  
4     ~~or subcontract to manufacture property for ultimate use in a Joint~~  
5     ~~Strike Fighter or a Crew Exploration Vehicle.~~

6     ~~(4) “Joint Strike Fighter” means the next generation air combat~~  
7     ~~strike aircraft developed and produced under the Joint Strike~~  
8     ~~Fighter program.~~

9     ~~(5) “Joint Strike Fighter program” means the multiservice,~~  
10    ~~multinational project conducted by the United States government~~  
11    ~~to develop and produce the next generation of air combat strike~~  
12    ~~aircraft.~~

13    ~~(6) “Crew Exploration Vehicle” means the next generation~~  
14    ~~spacecraft being planned by the National Aeronautics and Space~~  
15    ~~Administration.~~

16    ~~(e) The credit allowed by this section shall not exceed ten~~  
17    ~~thousand dollars (\$10,000) per year, per qualified employee. For~~  
18    ~~employees that are qualified employees for part of a taxable year,~~  
19    ~~the credit shall not exceed ten thousand dollars (\$10,000) multiplied~~  
20    ~~by a fraction, the numerator of which is the number of months of~~  
21    ~~the taxable year that the employee is a qualified employee and the~~  
22    ~~denominator of which is 12.~~

23    ~~(d) In the case where the credit allowed by this section exceeds~~  
24    ~~the “net tax,” the excess may be carried over to reduce the “net~~  
25    ~~tax” in the following year, and the succeeding years if necessary,~~  
26    ~~until the credit is exhausted.~~

27    ~~(e) No credit shall be allowed unless the credit is reflected within~~  
28    ~~the bid upon which the qualified taxpayer’s contract or subcontract~~  
29    ~~to manufacture property for ultimate use in a Joint Strike Fighter~~  
30    ~~or a Crew Exploration Vehicle is based by reducing the amount~~  
31    ~~of the bid by the amount of the credit allowable.~~

32    ~~(f) All references to the credit and ultimate cost reductions~~  
33    ~~incorporated into any successful bid that was awarded a contract~~  
34    ~~or subcontract and for which a qualified taxpayer is making a claim~~  
35    ~~shall be made available to the Franchise Tax Board upon request.~~

36    ~~(g) This section shall remain in effect only until December 1,~~  
37    ~~2017, and as of that date is repealed.~~

38    ~~SEC. 6. Section 17053.37 is added to the Revenue and Taxation~~  
39    ~~Code, to read:~~

1     ~~17053.37.— (a) For each taxable year beginning on or after~~  
2     ~~January 1, 2007, and before January 1, 2017, a qualified taxpayer~~  
3     ~~shall be allowed as a credit against the “net tax,” as defined in~~  
4     ~~Section 17039, an amount equal to 10 percent of the qualified cost~~  
5     ~~of qualified property that is placed in service in this state.~~

6     ~~(b) (1) For purposes of this section, “qualified cost” means any~~  
7     ~~costs that satisfy each of the following conditions:~~

8     ~~(A) Except as otherwise provided in this subparagraph, is a cost~~  
9     ~~paid or incurred by the qualified taxpayer for the construction,~~  
10    ~~reconstruction, or acquisition of qualified property on or after~~  
11    ~~January 1, 2007, and before January 1, 2017. In the case of any~~  
12    ~~qualified property constructed, reconstructed, or acquired by the~~  
13    ~~qualified taxpayer, or any person related to the qualified taxpayer~~  
14    ~~within the meaning of Section 267 or 707 of the Internal Revenue~~  
15    ~~Code, pursuant to a binding contract in existence on or before~~  
16    ~~January 1, 2007, costs paid pursuant to that contract shall be subject~~  
17    ~~to allocation as follows. Contract costs shall be allocated to~~  
18    ~~qualified property based on a ratio of costs actually paid prior to~~  
19    ~~January 1, 2007, and total contract costs actually paid. “Cost paid”~~  
20    ~~shall include, without limitation, contractual deposits and option~~  
21    ~~payments. To the extent of costs allocated, whether or not currently~~  
22    ~~deductible or depreciable for tax purposes, to a period prior to~~  
23    ~~January 1, 2007, the cost shall be deemed allocated to property~~  
24    ~~acquired before January 1, 2007, and is thus not a “qualified cost.”~~

25    ~~(B) Except for capitalized labor costs as described in~~  
26    ~~subparagraph (B) of paragraph (1) of subdivision (d), is an amount~~  
27    ~~upon which the qualified taxpayer has paid, directly or indirectly,~~  
28    ~~as a separately stated contract amount or as determined from the~~  
29    ~~records of the qualified taxpayer, sales or use tax under Part 1~~  
30    ~~(commencing with Section 6001).~~

31    ~~(C) Is an amount properly chargeable to the capital account of~~  
32    ~~the qualified taxpayer.~~

33    ~~(2) (A) For purposes of this subdivision, any contract entered~~  
34    ~~into on or after January 1, 2007, that is a successor or replacement~~  
35    ~~contract to a contract that was binding before January 1, 2007,~~  
36    ~~shall be treated as a binding contract in existence before January~~  
37    ~~1, 2007.~~

38    ~~(B) If a successor or replacement contract is entered into on or~~  
39    ~~after January 1, 2007, and the subject of the successor or~~  
40    ~~replacement contract relates both to amounts for the construction,~~

1 reconstruction, or acquisition of qualified property described in  
2 the original binding contract and to costs for the construction;  
3 reconstruction, or acquisition of qualified property not described  
4 in the original binding contract, then the portion of those amounts  
5 described in the successor or replacement contract that were not  
6 described in the original binding contract shall not be treated as  
7 costs paid or incurred pursuant to a binding contract in existence  
8 on or prior to January 1, 2007, under subparagraph (A) of paragraph  
9 (1).

10 (3) (A) For purposes of this section, an option contract in  
11 existence before January 1, 2007, under which a qualified taxpayer  
12 (or any other person related to the qualified taxpayer within the  
13 meaning of Section 267 or 707 of the Internal Revenue Code) had  
14 an option to acquire qualified property, shall be treated as a binding  
15 contract under the rules in paragraph (2). For purposes of this  
16 subparagraph, an option contract shall not include an option under  
17 which the optionholder will forfeit an amount less than 10 percent  
18 of the fixed option price in the event the option is not exercised.

19 (B) For purposes of this section, a contract shall be treated as  
20 binding even if the contract is subject to a condition.

21 (c) (1) For purposes of this section, “qualified taxpayer” means  
22 any taxpayer under an initial contract or subcontract to manufacture  
23 property for ultimate use in a Joint Strike Fighter or a Crew  
24 Exploration Vehicle.

25 (2) In the case of any passthrough entity, the determination of  
26 whether a taxpayer is a qualified taxpayer under this section shall  
27 be made at the entity level and any credit under this section or  
28 Section 23637 shall be allowed to the passthrough entity and passed  
29 through to the partners or shareholders in accordance with  
30 applicable provisions of Part 10 (commencing with Section 17001)  
31 or Part 11 (commencing with Section 23001). For purposes of this  
32 paragraph, the term “passthrough entity” means any partnership  
33 or “S” corporation.

34 (3) The Franchise Tax Board may prescribe regulations to carry  
35 out the purposes of this section, including any regulations necessary  
36 to prevent the avoidance of the effect of this section through  
37 splitups, shell corporations, partnerships, tiered ownership  
38 structures, sale-leaseback transactions, or otherwise.

39 (d) (1) For purposes of this section, “qualified property” means  
40 property that is described as either of the following:

~~(A) Tangible personal property that is defined in Section 1245(a)(3)(A) of the Internal Revenue Code for use by a qualified taxpayer primarily in qualified activities to manufacture a product for ultimate use in a Joint Strike Fighter or a Crew Exploration Vehicle.~~

~~(B) The value of any capitalized labor costs that are direct costs as defined in Section 263A of the Internal Revenue Code allocable to the construction or modification of property described in subparagraph (A).~~

~~(2) Qualified property does not include any of the following:~~

~~(A) Furniture.~~

~~(B) Inventory.~~

~~(C) Equipment used to store finished products that have completed the manufacturing process.~~

~~(D) Any tangible personal property that is used in administration, general management, or marketing.~~

~~(e) For purposes of this section:~~

~~(1) “Crew Exploration Vehicle” means the next generation spacecraft being planned by the National Aeronautics and Space Administration.~~

~~(2) “Fabricating” means to make, build, create, produce, or assemble components or property to work in a new or different manner.~~

~~(3) “Joint Strike Fighter” means the next generation air combat strike aircraft developed and produced under the Joint Strike Fighter program.~~

~~(4) “Joint Strike Fighter program” means the multiservice, multinational project conducted by the United States government to develop and produce the next generation of air combat strike aircraft.~~

~~(5) “Manufacturing” means the activity of converting or conditioning property by changing the form, composition, quality, or character of the property for ultimate use in a Joint Strike Fighter or a Crew Exploration Vehicle. Manufacturing includes any improvements to tangible personal property that result in a greater service life or greater functionality than that of the original property.~~

~~(6) “Primarily” means tangible personal property used 50 percent or more of the time in an activity described in subparagraph (A) of paragraph (1) of subdivision (d).~~

1     (7) “Process” means the period beginning at the point at which  
2     any raw materials are received by the qualified taxpayer and  
3     introduced into the manufacturing, processing, or fabricating  
4     activity of the qualified taxpayer and ending at the point at which  
5     the manufacturing, processing, or fabricating activity of the  
6     qualified taxpayer has altered tangible personal property to its  
7     completed form, including packaging, if required. Raw materials  
8     shall be considered to have been introduced into the process when  
9     the raw materials are stored on the same premises where the  
10    qualified taxpayer’s manufacturing, processing, or fabricating  
11    activity is conducted. Raw materials that are stored on premises  
12    other than where the qualified taxpayer’s manufacturing,  
13    processing, or fabricating activity is conducted, shall not be  
14    considered to have been introduced into the manufacturing,  
15    processing, or fabricating process.

16    (8) “Processing” means the physical application of the materials  
17    and labor necessary to modify or change the characteristics of  
18    property.

19    (9) “Qualified activities” means manufacturing, processing, or  
20    fabricating of property, beginning at the point at which any raw  
21    materials are received by the qualified taxpayer and introduced  
22    into the process and ending at the point at which the manufacturing,  
23    processing, or fabricating has altered tangible personal property  
24    to its completed form, including packaging, if required.

25    (f) The credit allowed under subdivision (a) shall apply to  
26    qualified property that is acquired by or subject to lease by a  
27    qualified taxpayer, subject to the following special rules:

28    (1) A lessor of qualified property, irrespective of whether the  
29    lessor is a qualified taxpayer, shall not be allowed the credit  
30    provided under subdivision (a) with respect to any qualified  
31    property leased to another qualified taxpayer.

32    (2) For purposes of paragraphs (2) and (3) of subdivision (b),  
33    “binding contract” includes any lease agreement with respect to  
34    the qualified property.

35    (3) (A) For purposes of determining the qualified cost paid or  
36    incurred by a lessee in any leasing transaction that is not treated  
37    as a sale under Part 1 (commencing with Section 6001), the  
38    following rules shall apply:

1 (i) Except as provided by subparagraph (C) of this paragraph,  
2 subparagraphs (A) and (C) of paragraph (1) of subdivision (b) shall  
3 not apply.

4 (ii) Except as provided in subparagraph (B) and clause (iii), the  
5 “qualified cost” upon which the lessee shall compute the credit  
6 provided under this section shall be equal to the original cost to  
7 the lessor, within the meaning of Section 18031, of the qualified  
8 property that is the subject of the lease.

9 (iii) The requirement of subparagraph (B) of paragraph (1) of  
10 subdivision (b) shall be treated as satisfied only if the lessor has  
11 made a timely election under either Section 6094.1 or subdivision  
12 (d) of Section 6244 and has paid sales tax reimbursement or use  
13 tax measured by the purchase price of the qualified property, within  
14 the meaning of paragraph (5) of subdivision (g) of Section 6006.  
15 For purposes of this subdivision, the amount of original cost to  
16 the lessor which may be taken into account under clause (ii) shall  
17 not exceed the purchase price upon which sales tax reimbursement  
18 or use tax has been paid under the preceding sentence.

19 (B) For purposes of applying subparagraph (A) only, the  
20 following special rules shall apply:

21 (i) The original cost to the lessor of the qualified property shall  
22 be reduced by the amount of any original cost of that property that  
23 was taken into account by a predecessor lessee in computing the  
24 credit allowable under this section.

25 (ii) Clause (i) shall not apply in any case where the predecessor  
26 lessee was required to recapture the credit provided under this  
27 section pursuant to the provisions of subdivision (g).

28 (iii) For purposes of this section only, in any case where a  
29 successor lessor has acquired qualified property from a predecessor  
30 lessor in a transaction not treated as a sale under Part 1  
31 (commencing with Section 6001) of Division 2, the original cost  
32 to the successor lessor of the qualified property shall be reduced  
33 by the amount of the original cost of the qualified property that  
34 was taken into account by any lessee of the predecessor lessor in  
35 computing the credit allowable under this section.

36 (C) In determining the original cost of any qualified property  
37 under this paragraph, only amounts paid or incurred by the lessor  
38 on or after January 1, 2007, and before January 1, 2017, shall be  
39 taken into account. In the case of any qualified property  
40 constructed, reconstructed, or acquired by a lessor pursuant to a

1 binding contract in existence on or prior to January 1, 2007, the  
2 allocation rule specified in subparagraph (A) of paragraph (1) of  
3 subdivision (b) shall apply in determining the original cost to the  
4 lessor of qualified property.

5 (D) Notwithstanding subparagraph (A), in the case of any leasing  
6 transaction for which the lessee is allowed the credit under this  
7 section and thereafter the lessee, or any party related to the lessee  
8 within the meaning of Section 267 or 318 of the Internal Revenue  
9 Code, acquires the qualified property from the lessor, or any  
10 successor lessor, within one year from the date the qualified  
11 property is first used by the lessee under the terms of the lease, the  
12 lessee's (or related party's) acquisition of the qualified property  
13 from the lessor, or successor lessor, shall be treated as a disposition  
14 by the lessee of the qualified property that was subject to the lease  
15 under subdivision (g).

16 (4) For purposes of determining the qualified cost paid or  
17 incurred by a lessee in any leasing transaction that is treated as a  
18 sale under Part 1 (commencing with Section 6001) of Division 2,  
19 the following rules shall apply:

20 (A) Subparagraph (A) of paragraph (1) of subdivision (b) shall  
21 be applied by substituting the term "purchase" for the term  
22 "construction, reconstruction, or acquisition."

23 (B) Subparagraph (C) of paragraph (1) of subdivision (b) shall  
24 apply.

25 (C) The requirement of subparagraph (B) of paragraph (1) of  
26 subdivision (b) shall be treated as satisfied at the time that either  
27 the lessor or the qualified taxpayer pays sales or use tax under Part  
28 1 (commencing with Section 6001) of Division 2.

29 (5) (A) In the case of any leasing transaction described in  
30 paragraph (3), the lessor shall provide a statement to the lessee  
31 specifying the amount of the lessor's original cost of the qualified  
32 property and the amount of that cost upon which a sales or use tax  
33 was paid within 45 days after the close of the lessee's taxable year  
34 in which the credit is allowable to the lessee under this section.

35 (B) The statement required under subparagraph (A) shall be  
36 made available to the Franchise Tax Board upon request.

37 (g) No credit shall be allowed if the qualified property is  
38 removed from the state, is disposed of to an unrelated party, or is  
39 used for any purpose not qualifying for the credit provided in this  
40 section in the same taxable year in which the taxpayer first places

~~the qualified property in service in this state. If any qualified property for which a credit is allowed pursuant to this section is thereafter removed from this state, disposed of to an unrelated party, or used for any purpose not qualifying for the credit provided in this section within one year from the date the taxpayer first places the qualified property in service in this state, the amount of the credit allowed by this section for that qualified property shall be recaptured by adding that credit amount to the net tax of the qualified taxpayer for the taxable year in which the qualified property is disposed of, removed, or put to an ineligible use.~~

~~(h) In the case where the credit allowed by this section exceeds the “net tax,” the excess may be carried over to reduce the “net tax” in the following year, and the succeeding years if necessary, until the credit is exhausted.~~

~~(i) (1) No credit shall be allowed under this section if a credit is claimed under Section 17053.49 in connection with the same property.~~

~~(2) No credit shall be allowed unless the credit is reflected within the bid upon which the qualified taxpayer’s contract or subcontract to manufacture property for ultimate use in a Joint Strike Fighter or a Crew Exploration Vehicle is based by reducing the amount of the bid by the amount of the credit allowable.~~

~~(j) All references to the credit and ultimate cost reductions incorporated into any successful bid that was awarded a contract or subcontract and for which a qualified taxpayer is making a claim shall be made available to the Franchise Tax Board upon request.~~

~~(k) This section shall remain in effect only until January 1, 2017, and as of that date is repealed.~~

~~SEC. 7. Section 17053.85 is added to the Revenue and Taxation Code, to read:~~

~~17053.85.—(a) (1) For taxable years beginning on or after January 1, 2007, subject to the limitation in paragraph (2), there shall be allowed to a qualified taxpayer, as designated by the California Film Commission pursuant to subdivision (h), that makes an irrevocable election pursuant to subdivision (h) to claim the credit authorized by this section, as a credit against the “net tax,” as defined in Section 17039, an amount equal to 12 percent of the qualified amount. A movie of the week and a miniseries, for which an executed licensing agreement from a network or basic~~



1 eable entity is provided, shall be entitled to an additional 3 percent  
2 of the qualified amount.

3 (2) ~~The credit allowed by paragraph (1) shall not exceed the~~  
4 ~~lesser of any of the following:~~

5 (A) ~~The amount of the credit allocated to the qualified taxpayer~~  
6 ~~by the California Film Commission based on the initial application.~~

7 (B) ~~The amount of the credit calculated based on actual~~  
8 ~~allowable expenditures on the qualified motion picture.~~

9 (C) ~~Three million dollars (\$3,000,000) per qualified motion~~  
10 ~~picture.~~

11 (b) ~~For purposes of this section:~~

12 (1) ~~“Ancillary product” means any article for sale to the public~~  
13 ~~that contains a portion of, or any element of, the motion picture.~~

14 (2) ~~“Budget” means an estimate of all expenses paid or incurred~~  
15 ~~during the production period of a motion picture. It shall be the~~  
16 ~~same budget used by the qualified taxpayer and production~~  
17 ~~company for all qualified motion picture purposes.~~

18 (3) ~~“Clip use” means a use of any portion of a motion picture,~~  
19 ~~other than the qualified motion picture, used in the qualified motion~~  
20 ~~picture.~~

21 (4) (A) ~~“Employee fringe benefits” means the amount allowable~~  
22 ~~as a deduction under this part to the qualified taxpayer involved~~  
23 ~~in the production of the qualified motion picture for any year during~~  
24 ~~the production period with respect to any of the following:~~

25 (i) ~~Employer contributions under any pension, profit-sharing,~~  
26 ~~annuity, or similar plan.~~

27 (ii) ~~Employer-provided coverage under any accident or health~~  
28 ~~plan for employees.~~

29 (iii) ~~The employer’s cost of life or disability insurance provided~~  
30 ~~to employees.~~

31 (B) ~~Any amount treated as wages under clause (i) of~~  
32 ~~subparagraph (A) of paragraph (21) shall not be taken into account~~  
33 ~~under this paragraph.~~

34 (5) ~~“Licensing” means any grant of rights to distribute the~~  
35 ~~qualified motion picture, in whole or in part.~~

36 (6) ~~“Movie of the week” and “miniseries” both mean a motion~~  
37 ~~picture, produced for initial exploitation on television, which~~  
38 ~~contains a scripted storyline requiring two or more consecutive~~  
39 ~~hours of programming.~~

1     ~~(7) “New to California” means a television series that has not~~  
2     ~~previously engaged in principal photography in this state, other~~  
3     ~~than for a production that is a pilot or presentation.~~

4     ~~(8) “New use” means any use of a motion picture in a medium~~  
5     ~~other than the medium for which it was initially created.~~

6     ~~(9) (A) “Postproduction” means the final activities in a qualified~~  
7     ~~motion picture’s production, including editing, foley recording,~~  
8     ~~automatic dialogue replacement, sound editing, scoring and music~~  
9     ~~editing, beginning and end credits, negative cutting, negative~~  
10    ~~processing and duplication, the addition of sound and visual effects,~~  
11    ~~soundmixing, film to tape transfers, encoding, and color correction.~~

12    ~~(B) “Postproduction” does not include the manufacture or~~  
13    ~~shipping of release prints.~~

14    ~~(10) “Preproduction” means the process of preparation for actual~~  
15    ~~physical production which begins after a qualified motion picture~~  
16    ~~has received a firm agreement of financial commitment, or is~~  
17    ~~greenlit, with, for example, the establishment of a dedicated~~  
18    ~~production office, the hiring of key crew members, and includes,~~  
19    ~~but is not limited to, activities that include location scouting and~~  
20    ~~execution of contracts with vendors of equipment and stage space.~~

21    ~~(11) “Principal photography” means the phase of production~~  
22    ~~during which the motion picture is actually shot, as distinguished~~  
23    ~~from preproduction and postproduction.~~

24    ~~(12) “Production accountant” means an employee of the~~  
25    ~~production company whose duties include some or all of the~~  
26    ~~following activities: oversight of production budgets, cost~~  
27    ~~reporting, order management, payment of expenses, and the review~~  
28    ~~of financial reports for accuracy and completeness.~~

29    ~~(13) “Production company” means a company primarily engaged~~  
30    ~~in qualified production activities that have been approved by the~~  
31    ~~California Film Commission.~~

32    ~~(14) “Production period” means the period of time in which the~~  
33    ~~preproduction, principal photography, and postproduction occurs~~  
34    ~~until the qualified motion picture is completed, as described in~~  
35    ~~clause (v) of subparagraph (C) of paragraph (18).~~

36    ~~(15) (A) “Qualified amount” means all of the following:~~

37    ~~(i) The total amount paid or incurred during the production~~  
38    ~~period for qualified wages with respect to the production of each~~  
39    ~~qualified motion picture.~~

1 ~~(ii) The total amount paid or incurred during the production~~  
2 ~~period for qualified property.~~

3 ~~(iii) Amounts paid or incurred for qualified wages and qualified~~  
4 ~~property related to the qualified motion picture for preproduction~~  
5 ~~costs that include set design and construction, props, wardrobe,~~  
6 ~~prosthetics, testing, and location scouting that are paid or incurred.~~  
7 ~~In the case of a television series described in clause (ii) of~~  
8 ~~subparagraph (C) of paragraph (18), the amounts paid or incurred~~  
9 ~~for the items described in this subparagraph shall be ratably~~  
10 ~~allocated among the episodes produced in the first season.~~

11 ~~(B) Notwithstanding subparagraph (A), the term “qualified~~  
12 ~~amount” shall not include any qualified wages paid or incurred~~  
13 ~~for services performed nor any qualified property purchased or~~  
14 ~~leased before January 1, 2007.~~

15 ~~(16) “Qualified entity” means a personal service corporation as~~  
16 ~~defined in Section 269A(b)(1) of the Internal Revenue Code, a~~  
17 ~~payroll services corporation, or any entity receiving qualified wages~~  
18 ~~with respect to services performed by a qualified individual.~~

19 ~~(17) (A) “Qualified individual” means any individual who~~  
20 ~~performs services during the production period in an activity related~~  
21 ~~to the production of a qualified motion picture.~~

22 ~~(B) “Qualified individual” shall not include either of the~~  
23 ~~following:~~

24 ~~(i) Any individual related to the qualified taxpayer as described~~  
25 ~~in subparagraph (A), (B), or (C) of Section 51(i)(1) of the Internal~~  
26 ~~Revenue Code.~~

27 ~~(ii) Any 5 percent owner, as defined in Section 416(i)(1)(B) of~~  
28 ~~the Internal Revenue Code, of the qualified taxpayer.~~

29 ~~(18) (A) “Qualified motion picture” means any motion picture~~  
30 ~~that is produced, adapted, or altered for exploitation in, on, or~~  
31 ~~through any medium or by any device, including, but not limited~~  
32 ~~to, a motion picture produced for exploitation in movie theaters,~~  
33 ~~through any form of television, videotapes, videocassettes, DVDs, or~~  
34 ~~any other digital format or on commercial carriers. “Qualified~~  
35 ~~motion picture” shall also include, but shall not be limited to, all~~  
36 ~~adapted versions thereof, whether adapted for exploitation in any~~  
37 ~~language, for any media, or otherwise.~~

38 ~~(B) (i) “Qualified motion picture” shall not include any motion~~  
39 ~~picture produced for private noncommercial use, such as weddings~~

1 or graduations, by students made as part of any educational course,  
2 or any motion picture produced for industrial purposes.

3 (ii) ~~“Qualified motion picture” shall not include a news program,~~  
4 ~~current events or public events program, talk show, game show,~~  
5 ~~sporting event or activity, awards show, telethon or other~~  
6 ~~production that solicits funds, reality television program, a feature~~  
7 ~~where 80 percent or more of the content consists of~~  
8 ~~computer-generated images, clip-based programming if more than~~  
9 ~~50 percent of the content is comprised of licensed footage,~~  
10 ~~documentaries, variety programs, daytime dramas, strip shows,~~  
11 ~~one-half-hour (air time) episodic television shows, or any~~  
12 ~~production that falls within the recordkeeping requirements of~~  
13 ~~Section 2257 of Title 18 of the United States Code.~~

14 (C) ~~To qualify as a “qualified motion picture,” all of the~~  
15 ~~following additional conditions shall be satisfied:~~

16 (i) ~~The qualified motion picture shall be a feature with a~~  
17 ~~minimum budget of three million dollars (\$3,000,000) and a~~  
18 ~~maximum budget of seventy-five million dollars (\$75,000,000),~~  
19 ~~or a movie of the week or miniseries with a minimum budget of~~  
20 ~~five hundred thousand dollars (\$500,000) and a maximum budget~~  
21 ~~of seventy-five million dollars (\$75,000,000).~~

22 (ii) ~~A qualified motion picture shall also include a single episode~~  
23 ~~in a single season, not to exceed 22 episodes per season, of a~~  
24 ~~television series new to California with a minimum budget of five~~  
25 ~~hundred thousand dollars (\$500,000) and a maximum budget of~~  
26 ~~one million eight hundred thousand dollars (\$1,800,000) per~~  
27 ~~episode. This clause shall only apply to the first three seasons of~~  
28 ~~a television series that is new to California.~~

29 (iii) ~~The actual expenses totaled at the completion of the~~  
30 ~~qualified motion picture must fall within the fiscal ranges~~  
31 ~~established in clause (i) or (ii) at the time of application to the~~  
32 ~~California Film Commission.~~

33 (iv) ~~At least 75 percent of the total days spent in principal~~  
34 ~~photography of a qualified motion picture occur wholly in~~  
35 ~~California.~~

36 (v) ~~Production of the qualified motion picture is completed~~  
37 ~~within 30 months of the date on which the qualified taxpayer’s~~  
38 ~~application was approved by the California Film Commission. For~~  
39 ~~the purposes of this section, a qualified motion picture is~~  
40 ~~“completed” when the process of postproduction has been finished,~~

1 and a final answer print or broadcast delivery air master of the  
2 qualified motion picture is produced:

3 (vi) Principal photography of the qualified motion picture begins  
4 within 180 days of the designation of the taxpayer as a qualified  
5 taxpayer by the California Film Commission.

6 (D) For the purposes of clauses (i) and (ii) of subparagraph (C),  
7 the following additional rules apply:

8 (i) In computing the total amounts paid or incurred for the  
9 production of a qualified motion picture, all amounts paid or  
10 incurred by all persons or entities that share in the costs of the  
11 qualified motion picture shall be aggregated.

12 (ii) In the case of a television series, described in clause (ii) of  
13 subparagraph (C), each episode shall be treated as a separate  
14 qualified motion picture.

15 (E) For purposes of computing the limitations under this  
16 paragraph, “wages” means all amounts described in subparagraph  
17 (A) of paragraph (21), provided that these amounts are paid for  
18 services performed or rendered within this state.

19 (19) (A) “Qualified property” means tangible personal property  
20 purchased or leased in California and is used primarily in the  
21 production of a qualified motion picture.

22 (B) “Qualified property” shall not include a story, script, or  
23 scenario to be used for a qualified motion picture, or the literary,  
24 dramatic, or musical material upon which the qualified motion  
25 picture is based or may be adapted, or any rights related to the  
26 foregoing.

27 (20) (A) “Qualified taxpayer” means an applicant who has been  
28 allocated tax credits by the California Film Commission pursuant  
29 to subdivision (h).

30 (B) (i) In the case of any passthrough entity, the determination  
31 of whether a taxpayer is a qualified taxpayer under this section  
32 shall be made at the entity level and any credit under this section  
33 is not allowed to the passthrough entity, but shall be passed through  
34 to the partners or shareholders in accordance with applicable  
35 provisions of Part 10 (commencing with Section 17001) or Part  
36 11 (commencing with Section 23001). For purposes of this  
37 paragraph, “passthrough entity” means any entity taxed as a  
38 partnership or “S” corporation.

39 (ii) In the case of an “S” corporation, the credit allowed under  
40 this section shall not be used by an “S” corporation as a credit

1 against a tax imposed under Chapter 4.5 (commencing with Section  
2 23800) of Part 11 of Division 2.

3 (21) (A) “Qualified wages” means all of the following:

4 (i) Any wages reported under Section 13050 of the  
5 Unemployment Insurance Code that were paid or incurred by the  
6 production company involved in the production of a qualified  
7 motion picture with respect to a qualified individual for services  
8 performed on the qualified motion picture production within this  
9 state.

10 (ii) The portion of any employee fringe benefits paid or incurred  
11 by the production company involved in the production of the  
12 qualified motion picture that are properly allocable to qualified  
13 wage amounts described in clause (i).

14 (iii) Any payments made to a qualified entity for services  
15 performed on a qualified motion picture in this state by qualified  
16 individuals within the meaning of paragraph (17).

17 (iv) Remuneration paid to an independent contractor, as  
18 described in Section 2750.5 of the Labor Code, who is a qualified  
19 individual for services performed within this state by that qualified  
20 individual.

21 (B) “Qualified wages” shall not include any of the following:

22 (i) Expenses, including wages, for legal or accounting services  
23 except production accountants.

24 (ii) Expenses, including wages, in excess of the first twenty-five  
25 thousand dollars (\$25,000) paid per person per qualified motion  
26 picture for writers, directors, music directors, music composers,  
27 music supervisors, producers, and performers, other than  
28 background actors with no scripted lines.

29 (iii) Expenses, including wages, related to new use, reuse, clip  
30 use, licensing, secondary markets, or residual compensation, or  
31 the creation of any ancillary product, including, but not limited to,  
32 a soundtrack album, toy, game, trailer, or teaser.

33 (iv) Expenses, including wages, paid or incurred with respect  
34 to acquisition, development, turnaround, or any rights thereto.

35 (v) Expenses, including wages, related to financing, overhead,  
36 marketing, promotion, or distribution of a qualified motion picture.

37 (22) “Residual compensation” means supplemental  
38 compensation paid at the time that a motion picture is exhibited  
39 through new use, reuse, clip use, or in secondary markets, as  
40 distinguished from payments made during production.

1     ~~(23) “Reuse” means any use of a qualified motion picture in the~~  
2 ~~same medium for which it was created, following the initial use~~  
3 ~~in that medium.~~

4     ~~(24) “Secondary markets” means media in which a qualified~~  
5 ~~motion picture is exhibited following the initial media in which it~~  
6 ~~is exhibited.~~

7     ~~(e) In the case where the credit allowed under this section~~  
8 ~~exceeds the “net tax,” the excess may be carried over to reduce~~  
9 ~~the “net tax” in the following year, and succeeding years if~~  
10 ~~necessary, until the credit has been exhausted.~~

11     ~~(d) No credit shall be allowed pursuant to this section unless~~  
12 ~~the qualified taxpayer substantiates, by adequate books and records~~  
13 ~~or by sufficient evidence corroborating his or her own statement,~~  
14 ~~that:~~

15     ~~(1) The qualified wages and the qualified property on which~~  
16 ~~the credit was calculated were actually paid or incurred in the~~  
17 ~~amount claimed. Substantiation of this item shall include proof~~  
18 ~~that the services were performed in California and the qualified~~  
19 ~~property was purchased or leased in California.~~

20     ~~(2) The motion picture was a qualified motion picture.~~  
21 ~~Substantiation of this item shall include, but is not limited to, the~~  
22 ~~following:~~

23     ~~(A) Identification of each qualified individual.~~

24     ~~(B) The specific start and end dates of production.~~

25     ~~(C) The total wages paid and amount and type of qualified~~  
26 ~~property purchased.~~

27     ~~(D) The amount of qualified wages paid to each qualified~~  
28 ~~individual.~~

29     ~~(E) Certification from the Director of the California Film~~  
30 ~~Commission that identifies the motion picture as a qualified motion~~  
31 ~~picture.~~

32     ~~(e) The Franchise Tax Board shall provide an annual listing to~~  
33 ~~the State Board of Equalization, in a form and manner agreed upon~~  
34 ~~by the Franchise Tax Board and the State Board of Equalization,~~  
35 ~~of the qualified taxpayers who, during that reporting period, have~~  
36 ~~claimed a credit under this section, including the amount of the~~  
37 ~~credit allowed to each qualified taxpayer.~~

38     ~~(f) Subdivision (e) of Section 19341, relating to interest on~~  
39 ~~overpayments, shall not apply to any return claiming a credit under~~  
40 ~~this section.~~

1     ~~(g) If the qualified taxpayer fails to attach the certification issued~~  
2     ~~by the California Film Commission in accordance with subdivision~~  
3     ~~(h), the credit shall be disallowed and assessed and collected under~~  
4     ~~Section 19051.~~

5     ~~(h) (1) For purposes of this section, the Director of the~~  
6     ~~California Film Commission shall do all of the following:~~

7     ~~(A) Allocate tax credits to applicants.~~

8     ~~(B) Establish a procedure for qualified taxpayers to file with~~  
9     ~~the California Film Commission a written application, on a form~~  
10    ~~jointly prescribed by the California Film Commission and the~~  
11    ~~Franchise Tax Board, for allocation of tax credits. The application~~  
12    ~~shall be filed under penalty of perjury and include, but not be~~  
13    ~~limited to, the following information:~~

14    ~~(i) The budget for the motion picture production.~~

15    ~~(ii) A one-line shooting schedule.~~

16    ~~(iii) A financing plan for the production.~~

17    ~~(iv) An application fee.~~

18    ~~(v) The copyright registration number for the screenplay, as~~  
19    ~~reflected on the certificate of registration issued under the authority~~  
20    ~~of Section 410 of Title 17 of the United States Code, relating to~~  
21    ~~registration of claim and issuance of certificate.~~

22    ~~(vi) Any other information deemed relevant by the California~~  
23    ~~Film Commission.~~

24    ~~(C) Establish a procedure for qualified taxpayers to make an~~  
25    ~~irrevocable election to claim the tax credit allocation as a credit~~  
26    ~~pursuant to this section or as a credit pursuant to Section 6902.5.~~

27    ~~(D) Determine and designate who is a qualified taxpayer meeting~~  
28    ~~the requirements of this section.~~

29    ~~(E) Process and approve, or reject, all applications on a~~  
30    ~~first-come, first-served basis.~~

31    ~~(F) Provide for the cancellation of the allocated credits, if~~  
32    ~~principal photography on the qualified motion picture does not~~  
33    ~~begin within 180 days after notification of the credit allocation by~~  
34    ~~the California Film Commission in accordance with subdivision~~  
35    ~~(i).~~

36    ~~(G) Establish specific audit requirements, in addition to those~~  
37    ~~provided under current law, that must be complied with prior to~~  
38    ~~the issuance of the certificate required by subparagraph (H), and~~  
39    ~~provide for the reallocation of previously approved credits that are~~



1 disallowed pursuant to the audit requirements, in accordance with  
2 subdivision (i):

3 (H) Issue a certificate to the qualified taxpayer setting forth the  
4 name of the qualified taxpayer, identification of the qualified  
5 motion picture, and the total amount of the tax credit allocated:

6 (2) ~~No later than \_\_\_\_\_ 2007, the California Film Commission~~  
7 ~~shall promulgate rules and regulations necessary to establish~~  
8 ~~procedures, processes, requirements, and rules identified in or~~  
9 ~~required to implement this section. Rules and regulations may be~~  
10 ~~adopted on an emergency basis if necessary to meet the March 1,~~  
11 ~~2008, deadline. The California Film Commission may amend these~~  
12 ~~rules and regulations as necessary. The California Film~~  
13 ~~Commission may adopt rules and regulations to more narrowly~~  
14 ~~define the terms listed in subdivision (b) to limit their meaning,~~  
15 ~~but may not expand the definition of any terms defined in~~  
16 ~~subdivision (b):~~

17 (i) The aggregate amount of credits that may be allocated in any  
18 calendar year pursuant to this section and Section 23685, and shall  
19 be an amount equal to the sum of all of the following:

20 (1) Ten million dollars (\$10,000,000) for each calendar quarter,  
21 and each calendar quarter thereafter.

22 (2) The unused credit ceiling, if any, for the preceding calendar  
23 quarter.

24 (3) ~~The amount of previously allocated credit cancelled or~~  
25 ~~disallowed in the preceding calendar quarter by reason of~~  
26 ~~subparagraph (F) or subparagraph (G) of paragraph (1) of~~  
27 ~~subdivision (h):~~

28 (j) The California Film Commission shall provide a list, at least  
29 annually, to the Franchise Tax Board, in the form and manner as  
30 shall be determined by the California Film Commission and the  
31 Franchise Tax Board, of the names, taxpayer identification  
32 numbers, including taxpayer identification numbers of each partner  
33 or shareholder, as applicable, the qualified motion pictures for  
34 which tax credit was allocated, and the total amount of the tax  
35 credit allocated to each qualified taxpayer.

36 (k) ~~This section shall remain in effect only until January 1, 2017,~~  
37 ~~and as of that date is repealed, unless a later enacted statute, that~~  
38 ~~is enacted before January 1, 2017, deletes or extends that date.~~

39 SEC. 8. ~~Section 17053.86 is added to the Revenue and Taxation~~  
40 ~~Code, to read:~~

~~17053.86.—(a) (1) For taxable years beginning on or after January 1, 2007, subject to the limitation in paragraph (2), there shall be allowed to a qualified commercial production company, as designated by the California Film Commission pursuant to subdivision (g), as a credit against the “net tax,” as defined in Section 17039, an amount equal to 12 percent of the incremental qualified production costs.~~

~~(2) The credit allowed by paragraph (1) shall not exceed the lesser of:~~

~~(A) Five hundred thousand dollars (\$500,000) per qualified production company per calendar year.~~

~~(B) The amount of the credit allocated by the California Film Commission to the qualified commercial production company pursuant to subdivision (g).~~

~~(b) For the purposes of this section:~~

~~(1) “Base year” is the taxable year preceding the taxable year for which the credit is claimed.~~

~~(2) (A) “Employee fringe benefits” means the amount allowable as a deduction under this part to the qualified commercial production company involved in the production of the qualified commercial for any year during the production period with respect to any of the following:~~

~~(i) Employer contributions under any pension, profit-sharing, annuity, or similar plan.~~

~~(ii) Employer-provided coverage under any accident or health plan for employees.~~

~~(iii) The employer’s cost of life or disability insurance provided to employees.~~

~~(B) Any amount treated as wages under clause (i) of subparagraph (A) of paragraph (10) shall not be taken into account under this paragraph.~~

~~(3) “Incremental qualified production costs” are any qualified production costs for the taxable year greater than the qualified production costs for the base year.~~

~~(4) “Principal photography” means the phase of production during which the qualified commercial is actually shot.~~

~~(5) “Postproduction” means the final activities in a qualified commercial’s production, including, but not limited to, offline editorial, online editorial, dailies, color correction, compositing, CGI, graphics, sound editorial, sound mixing, sound design,~~

1 automated dialogue replacement, foley recording, music  
2 composition and scoring, and duplication associated with the above  
3 process.

4 (6) (A) “Qualified commercial” means a commercial or  
5 advertisement composed of moving images and sounds that is  
6 recorded on film, videotape, or other digital medium, created for  
7 display on a network, regional channel, or cable where 75 percent  
8 of the total production days spent in principal photography occur  
9 wholly in California.

10 (B) “Qualified commercial” shall not include any program length  
11 production with an advertising component including a documentary  
12 length commercial, an infomercial, news, or current affairs  
13 program, interview or talk program, network promotion (short  
14 form content intended to promote other programming), sporting  
15 event, game show, award ceremony, daytime drama, reality  
16 entertainment programming or program intended primarily for  
17 industrial, corporate, or institutional end users, fundraising or  
18 political commercial, a program consisting primarily of stock  
19 footage, a program produced by an organization organized under  
20 Section 527 of the Internal Revenue Code, or any production that  
21 falls within the recordkeeping requirements of Section 2257 of  
22 Title 18 of the United States Code.

23 (7) (A) “Qualified commercial production company” means a  
24 taxpayer, allocated tax credits by the California Film Commission  
25 pursuant to subdivision (g), that is principally engaged in the  
26 production of a qualified commercial and has control over the  
27 selection of production location, deployment, or management of  
28 the production equipment, and directly employs the production  
29 crew on the qualified commercial, or is a taxpayer who provides  
30 postproduction services on a qualified commercial.

31 (B) (i) In the case of any passthrough entity, the determination  
32 of whether a taxpayer is a qualified commercial production  
33 company under this section shall be made at the entity level and  
34 any credit under this section is not allowed to the passthrough  
35 entity, but shall be passed through to the partners or shareholders  
36 in accordance with applicable provisions of Part 10 (commencing  
37 with Section 17001) or Part 11 (commencing with Section 23001).  
38 For the purposes of this paragraph, “passthrough entity” means  
39 any entity taxed as a partnership or “S” corporation.

~~(ii) In the case of an “S” corporation, the credit allowed under this section shall not be used by an “S” corporation as a credit against a tax imposed under Chapter 4.5 (commencing with Section 23800) of Part 11 of Division 2.~~

~~(8) (A) “Qualified individual” means any individual who performs services during the production period in an activity related to the production of a qualified commercial.~~

~~(B) “Qualified individual” shall not include either of the following:~~

~~(i) Any individual related to the qualified commercial production company as described in subparagraph (A), (B), (C), or Section 51(i)(1) of the Internal Revenue Code.~~

~~(ii) Any 5 percent owner, as defined in Section 416(i)(1)(B) of the Internal Revenue Code, of the qualified commercial production company.~~

~~(9) “Qualified production costs” means all of the following:~~

~~(A) Costs for tangible property used and services performed directly and predominately in the production of a qualified commercial.~~

~~(B) Costs for qualified wages, technical and crew production costs, allocable portions of depreciation on equipment directly used in production, rental or other expenditures for commercial production facilities, props, makeup, wardrobe, film processing, camera rental, sound recording, set construction, lighting, on-location meals, and lodging.~~

~~(C) Costs for equipment and services required to complete postproduction of the qualified commercial.~~

~~(D) “Qualified production costs” does not include costs for story, script, or scenario to be used for a qualified commercial, or any qualified wages paid or incurred before January 1, 2007.~~

~~(10) (A) “Qualified wages” means all of the following:~~

~~(i) Any wages reported under Section 13050 of the Unemployment Insurance Code that were paid or incurred by the qualified commercial production company involved in the production of a qualified commercial with respect to a qualified individual for services performed on the qualified commercial production within this state.~~

~~(ii) The portion of any employee fringe benefits paid or incurred by the qualified commercial production company involved in the~~

1 production of a qualified commercial that are properly allocated  
2 to qualified wage amounts described in clause (i).

3 (iii) ~~Remuneration paid to a qualified individual for services~~  
4 ~~performed within this state by that qualified individual.~~

5 (iv) ~~Remuneration paid to an independent contractor, as~~  
6 ~~described in Section 2750.5 of the Labor Code, who is a qualified~~  
7 ~~individual for services performed in this state by that qualified~~  
8 ~~individual.~~

9 (B) ~~“Qualified wages” shall not include wages, salaries, or other~~  
10 ~~compensation for writers, directors, music directors, producers,~~  
11 ~~and performers (other than background actors with no scripted~~  
12 ~~lines who are employed by a qualified commercial production~~  
13 ~~company).~~

14 (c) ~~In the case where the credit allowed under this section~~  
15 ~~exceeds the “net tax,” the excess may be carried over to reduce~~  
16 ~~the “net tax” in the following year, and succeeding years if~~  
17 ~~necessary, until the credit has been exhausted.~~

18 (d) ~~No credit shall be allowed pursuant to this section unless~~  
19 ~~the qualified commercial production company substantiates, by~~  
20 ~~adequate books and records or by sufficient evidence corroborating~~  
21 ~~his or her own statement, that:~~

22 (1) ~~The incremental qualified production costs upon which the~~  
23 ~~credit was calculated were actually paid or incurred in the amount~~  
24 ~~claimed.~~

25 (2) ~~The commercial was a qualified commercial. Substantiation~~  
26 ~~of this item shall include, but is not limited to, the following:~~

27 (A) ~~Identification of each qualified individual.~~

28 (B) ~~The specific start and end dates of production.~~

29 (C) ~~The total wages paid.~~

30 (D) ~~The amount of qualified wages paid to each qualified~~  
31 ~~individual.~~

32 (E) ~~Certification from the Director of the California Film~~  
33 ~~Commission as required in subdivision (g).~~

34 (e) ~~Subdivision (c) of Section 19341, relating to interest on~~  
35 ~~overpayments, shall not apply to any return claiming a credit under~~  
36 ~~this section.~~

37 (f) ~~If the qualified commercial production company fails to~~  
38 ~~attach the certification issued by the Director of the California~~  
39 ~~Film Commission, in accordance with subdivision (g), the credit~~

1 shall be disallowed and assessed and collected under Section  
2 19051.

3 (g) (1) For purposes of this section, the Director of the  
4 California Film Commission shall do all of the following:

5 (A) Allocate tax credits to applicants, including establishing a  
6 procedure to allocate tax credits among qualified commercial  
7 production companies pursuant to paragraph (2) of subdivision  
8 (h).

9 (B) Establish a procedure for qualified commercial production  
10 companies to file with the California Film Commission a written  
11 application, on a form jointly prescribed by the California Film  
12 Commission and the Franchise Tax Board, for allocation of tax  
13 credits. The application shall be filed under penalty of perjury and  
14 include, but not be limited to, the following information:

15 (i) The qualified production costs for the base year.

16 (ii) The qualified production costs for the taxable year in which  
17 the credit is claimed.

18 (iii) An application fee.

19 (iv) Any other information deemed relevant by the California  
20 Film Commission.

21 (C) Determine and designate who is a qualified commercial  
22 production company meeting the requirements of this section.

23 (D) Process and approve, or reject, all applications.

24 (E) Establish specific audit requirements, in addition to those  
25 provided under current law, that must be complied with prior to  
26 the issuance of the certificate required by subparagraph (F), and  
27 provide for the reallocation of previously approved credits that are  
28 disallowed pursuant to the audit requirements, in accordance with  
29 subdivision (h).

30 (F) Issue a certificate to the qualified taxpayer setting forth the  
31 name of the qualified taxpayer and the total amount of the tax  
32 credit allocated.

33 (2) No later than \_\_\_\_\_ 2007, the California Film Commission  
34 shall promulgate rules and regulations necessary to establish  
35 procedures, processes, requirements, and rules identified in or  
36 required to implement this section. Rules and regulations may be  
37 adopted on an emergency basis if necessary to meet the March 1,  
38 2008, deadline. The California Film Commission may amend these  
39 rules and regulations as necessary. The California Film  
40 Commission may adopt rules and regulations to more narrowly

1 ~~define the terms listed in subdivision (b) to limit their meaning,~~  
2 ~~but may not expand the definition of any terms defined in~~  
3 ~~subdivision (b).~~

4 ~~(h) (1) The aggregate amount of credits that may be allocated~~  
5 ~~in any calendar year pursuant to this section and Section 23686~~  
6 ~~shall be an amount equal to the sum of all of the following:~~

7 ~~(A) Twenty million dollars (\$20,000,000) for the 2008 calendar~~  
8 ~~year, and each calendar year thereafter.~~

9 ~~(B) The unused credit ceiling, if any, for the preceding calendar~~  
10 ~~years.~~

11 ~~(C) The amount of previously allocated credit canceled or~~  
12 ~~disallowed in the calendar year by reason of subparagraph (E) of~~  
13 ~~paragraph (1) of subdivision (g).~~

14 ~~(2) If the amount allocable to qualified commercial production~~  
15 ~~companies exceeds the aggregate amount of credits that may be~~  
16 ~~allocated in any calendar year, the credits shall be distributed to~~  
17 ~~qualified commercial production companies as follows:~~

18 ~~(A) The California Film Commission shall allocate the credits~~  
19 ~~on a pro rata basis to qualified commercial production companies~~  
20 ~~for the designated period.~~

21 ~~(B) The California Film Commission will compute the pro rata~~  
22 ~~allocation based on submitted applications from all qualified~~  
23 ~~commercial production companies within 120 days of the~~  
24 ~~application due date.~~

25 ~~(i) The California Film Commission shall provide a list, at least~~  
26 ~~annually, to the Franchise Tax Board, in the form and manner as~~  
27 ~~shall be determined by the California Film Commission and the~~  
28 ~~Franchise Tax Board, of the names, taxpayer identification~~  
29 ~~numbers, including taxpayer identification numbers of each partner~~  
30 ~~or shareholder, as applicable, the qualified motion pictures for~~  
31 ~~which tax credit was allocated, and the total amount of the tax~~  
32 ~~credit allocated to each qualified taxpayer.~~

33 ~~(j) This section shall remain in effect only until January 1, 2017,~~  
34 ~~and as of that date is repealed, unless a later enacted statute, that~~  
35 ~~is enacted before January 1, 2017, deletes or extends that date.~~

36 ~~SEC. 9.~~

37 ~~SEC. 3. Section 23609 of the Revenue and Taxation Code is~~  
38 ~~amended to read:~~

39 ~~23609. For each taxable year beginning on or after January 1,~~  
40 ~~1987, there shall be allowed as a credit against the "tax" (as defined~~

1 by Section 23036) an amount determined in accordance with  
2 Section 41 of the Internal Revenue Code, except as follows:  
3 (a) For each taxable year beginning before January 1, 1997,  
4 both of the following modifications shall apply:  
5 (1) The reference to “20 percent” in Section 41(a)(1) of the  
6 Internal Revenue Code is modified to read “8 percent.”  
7 (2) The reference to “20 percent” in Section 41(a)(2) of the  
8 Internal Revenue Code is modified to read “12 percent.”  
9 (b) (1) For each taxable year beginning on or after January 1,  
10 1997, and before January 1, 1999, both of the following  
11 modifications shall apply:  
12 (A) The reference to “20 percent” in Section 41(a)(1) of the  
13 Internal Revenue Code is modified to read “11 percent.”  
14 (B) The reference to “20 percent” in Section 41(a)(2) of the  
15 Internal Revenue Code is modified to read “24 percent.”  
16 (2) For each taxable year beginning on or after January 1, 1999,  
17 and before January 1, 2000, both of the following shall apply:  
18 (A) The reference to “20 percent” in Section 41(a)(1) of the  
19 Internal Revenue Code is modified to read “12 percent.”  
20 (B) The reference to “20 percent” in Section 41(a)(2) of the  
21 Internal Revenue Code is modified to read “24 percent.”  
22 (3) For each taxable year beginning on or after January 1, 2000,  
23 and before January 1, 2007, both of the following shall apply:  
24 (A) The reference to “20 percent” in Section 41(a)(1) of the  
25 Internal Revenue Code is modified to read “15 percent.”  
26 (B) The reference to “20 percent” in Section 41(a)(2) of the  
27 Internal Revenue Code is modified to read “24 percent.”  
28 (4) For each taxable year beginning on or after January 1, 2007,  
29 both of the following shall apply:  
30 (A) The reference to “20 percent” in Section 41(a)(1) of the  
31 ~~Internal Revenue Code is modified to read “16 percent.”~~ *Internal*  
32 *Revenue Code shall apply.*  
33 (B) The reference to “20 percent” in Section 41(a)(2) of the  
34 Internal Revenue Code is modified to read “24 percent.”  
35 (c) (1) With respect to any expense paid or incurred after the  
36 operative date of Section 6378, Section 41(b)(1) of the Internal  
37 Revenue Code is modified to exclude from the definition of  
38 “qualified research expense” any amount paid or incurred for  
39 tangible personal property that is eligible for the exemption from  
40 sales or use tax under Section 6378.



1 (2) “Qualified research” and “basic research” shall include only  
2 research conducted in California.

3 (d) The provisions of Section 41(e)(7)(A) of the Internal  
4 Revenue Code, shall be modified so that “basic research,” for  
5 purposes of this section, includes any basic or applied research  
6 including scientific inquiry or original investigation for the  
7 advancement of scientific or engineering knowledge or the  
8 improved effectiveness of commercial products, except that the  
9 term does not include any of the following:

10 (1) Basic research conducted outside California.

11 (2) Basic research in the social sciences, arts, or humanities.

12 (3) Basic research for the purpose of improving a commercial  
13 product if the improvements relate to style, taste, cosmetic, or  
14 seasonal design factors.

15 (4) Any expenditure paid or incurred for the purpose of  
16 ascertaining the existence, location, extent, or quality of any deposit  
17 of ore or other mineral (including oil and gas).

18 (e) (1) In the case of a taxpayer engaged in any  
19 biopharmaceutical research activities that are described in Codes  
20 2833 to 2836, inclusive, or any research activities that are described  
21 in Codes 3826, 3829, or 3841 to 3845, inclusive, of the Standard  
22 Industrial Classification (SIC) Manual published by the United  
23 States Office of Management and Budget, 1987 edition, or any  
24 other biotechnology research and development activities, the  
25 provisions of Section 41(e)(6) of the Internal Revenue Code shall  
26 be modified to include both of the following:

27 (A) A qualified organization as described in Section  
28 170(b)(1)(A)(iii) of the Internal Revenue Code and owned by an  
29 institution of higher education as described in Section 3304(f) of  
30 the Internal Revenue Code.

31 (B) A charitable research hospital owned by an organization  
32 that is described in Section 501(c)(3) of the Internal Revenue Code,  
33 is exempt from taxation under Section 501(a) of the Internal  
34 Revenue Code, is not a private foundation, is designated a  
35 “specialized laboratory cancer center,” and has received Clinical  
36 Cancer Research Center status from the National Cancer Institute.

37 (2) For purposes of this subdivision:

38 (A) “Biopharmaceutical research activities” means those  
39 activities that use organisms or materials derived from organisms,  
40 and their cellular, subcellular, or molecular components, in order

1 to provide pharmaceutical products for human or animal  
2 therapeutics and diagnostics. Biopharmaceutical activities make  
3 use of living organisms to make commercial products, as opposed  
4 to pharmaceutical activities that make use of chemical compounds  
5 to produce commercial products.

6 (B) “Other biotechnology research and development activities”  
7 means research and development activities consisting of the  
8 application of recombinant DNA technology to produce  
9 commercial products, as well as research and development  
10 activities regarding pharmaceutical delivery systems designed to  
11 provide a measure of control over the rate, duration, and site of  
12 pharmaceutical delivery.

13 (f) In the case where the credit allowed by this section exceeds  
14 the “tax,” the excess may be carried over to reduce the “tax” in  
15 the following year, and succeeding years if necessary, until the  
16 credit has been exhausted.

17 (g) For each taxable year beginning on or after January 1, 1998,  
18 the reference to “Section 501(a)” in Section 41(b)(3)(C) of the  
19 Internal Revenue Code, relating to contract research expenses, is  
20 modified to read “this part or Part 10 (commencing with Section  
21 17001).”

22 (h) (1) For each taxable year beginning on or after January 1,  
23 2000, and before January 1, 2007:

24 (A) The reference to “2.65 percent” in Section 41(c)(4)(A)(i)  
25 of the Internal Revenue Code is modified to read “one and  
26 forty-nine hundredths of one percent.”

27 (B) The reference to “3.2 percent” in Section 41(c)(4)(A)(ii) of  
28 the Internal Revenue Code is modified to read “one and  
29 ninety-eight hundredths of one percent.”

30 (C) The reference to “3.75 percent” in Section 41(c)(4)(A)(iii)  
31 of the Internal Revenue Code is modified to read “two and  
32 forty-eight hundredths of one percent.”

33 ~~(2) For each taxable year beginning on or after January 1, 2007,~~  
34 ~~the following apply:~~

35 ~~(A) The reference to “2.65 percent” in Section 41(c)(4)(A)(i)~~  
36 ~~of the Internal Revenue Code is modified to read “two percent.”~~

37 ~~(B) The reference to “3.2 percent” in Section 41(c)(4)(A)(ii) of~~  
38 ~~the Internal Revenue Code is modified to read “two and one-half~~  
39 ~~percent.”~~

1     ~~(C) The reference to “3.75 percent” in Section 41(c)(4)(A)(iii)~~  
2     ~~of the Internal Revenue Code is modified to read “three percent.”~~

3     ~~(2) For each taxable year beginning on or after January 1,~~  
4     ~~2007, Section 41(c)(4) of the Internal Revenue Code, relating to~~  
5     ~~the election of the alternative incremental credit, shall apply.~~

6     ~~(3) Section 41(c)(4)(B) shall not apply and in lieu thereof an~~  
7     ~~election under Section 41(c)(4)(A) of the Internal Revenue Code~~  
8     ~~may be made for any taxable year of the taxpayer beginning on or~~  
9     ~~after January 1, 1998. That election shall apply to the taxable year~~  
10    ~~for which made and all succeeding taxable years unless revoked~~  
11    ~~with the consent of the Franchise Tax Board.~~

12    ~~(4) Section 41(c)(6) of the Internal Revenue Code, relating to~~  
13    ~~gross receipts, is modified to take into account only those gross~~  
14    ~~receipts from the sale of property held primarily for sale to~~  
15    ~~customers in the ordinary course of the taxpayer’s trade or business~~  
16    ~~that is delivered or shipped to a purchaser within this state,~~  
17    ~~regardless of f.o.b. point or any other condition of the sale.~~

18    ~~(i) Section 41(h) of the Internal Revenue Code, relating to~~  
19    ~~termination, shall not apply.~~

20    ~~(j) Section 41(g) of the Internal Revenue Code, relating to~~  
21    ~~special rule for passthrough of credit, is modified by each of the~~  
22    ~~following:~~

23    ~~(1) The last sentence shall not apply.~~

24    ~~(2) If the amount determined under Section 41(a) of the Internal~~  
25    ~~Revenue Code for any taxable year exceeds the limitation of~~  
26    ~~Section 41(g) of the Internal Revenue Code, that amount may be~~  
27    ~~carried over to other taxable years under the rules of subdivision~~  
28    ~~(f), except that the limitation of Section 41(g) of the Internal~~  
29    ~~Revenue Code shall be taken into account in each subsequent~~  
30    ~~taxable year.~~

31    ~~SEC. 10.—Section 23636 is added to the Revenue and Taxation~~  
32    ~~Code, to read:~~

33    ~~23636. (a) For each taxable year beginning on or after January~~  
34    ~~1, 2007, and before January 1, 2017, a qualified taxpayer shall be~~  
35    ~~allowed as a credit against the “tax,” as defined in Section 23036,~~  
36    ~~an amount equal to the following:~~

37    ~~(1) Fifty percent of qualified wages paid or incurred during any~~  
38    ~~taxable year beginning on or after January 1, 2007, and before~~  
39    ~~January 1, 2010.~~

1     ~~(2) Forty percent of qualified wages paid or incurred during any~~  
2     ~~taxable year beginning on or after January 1, 2010, and before~~  
3     ~~January 1, 2012.~~

4     ~~(3) Thirty percent of the qualified wages paid or incurred during~~  
5     ~~any taxable year beginning on or after January 1, 2012, and before~~  
6     ~~January 1, 2014.~~

7     ~~(4) Twenty percent of the qualified wages paid or incurred~~  
8     ~~during any taxable year beginning on or after January 1, 2014, and~~  
9     ~~before January 1, 2016.~~

10    ~~(5) Ten percent of the qualified wages paid or incurred during~~  
11    ~~any taxable year beginning on or after January 1, 2016, and before~~  
12    ~~January 1, 2017.~~

13    ~~(b) For purposes of this section:~~

14    ~~(1) (A) “Qualified taxpayer” means any taxpayer under an~~  
15    ~~initial contract or subcontract to manufacture property for ultimate~~  
16    ~~use in a Joint Strike Fighter or a Crew Exploration Vehicle.~~

17    ~~(B) In the case of any passthrough entity, the determination of~~  
18    ~~whether a taxpayer is a qualified taxpayer under this section shall~~  
19    ~~be made at the entity level and any credit under this section or~~  
20    ~~Section 17053.36 shall be allowed to the passthrough entity and~~  
21    ~~passed through to the partners or shareholders in accordance with~~  
22    ~~applicable provisions of Part 10 (commencing with Section 17001)~~  
23    ~~or this part. For purposes of this paragraph, “passthrough entity”~~  
24    ~~means any partnership or “S” corporation.~~

25    ~~(2) “Qualified wages” means that portion of wages paid or~~  
26    ~~incurred by the qualified taxpayer during the taxable year with~~  
27    ~~respect to qualified employees that are direct costs as defined in~~  
28    ~~Section 263A of the Internal Revenue Code allocable to property~~  
29    ~~manufactured in this state by the qualified taxpayer for ultimate~~  
30    ~~use in a Joint Strike Fighter or a Crew Exploration Vehicle.~~

31    ~~(3) “Qualified employee” means an individual whose services~~  
32    ~~for the qualified taxpayer are performed in this state and are at~~  
33    ~~least 90 percent directly related to the qualified taxpayer’s contract~~  
34    ~~or subcontract to manufacture property for ultimate use in a Joint~~  
35    ~~Strike Fighter or a Crew Exploration Vehicle.~~

36    ~~(4) “Joint Strike Fighter” means the next generation air combat~~  
37    ~~strike aircraft developed and produced under the Joint Strike~~  
38    ~~Fighter program.~~

39    ~~(5) “Joint Strike Fighter program” means the multiservice,~~  
40    ~~multinational project conducted by the United States government~~

1 to develop and produce the next generation of air combat strike  
2 aircraft.

3 (6) “Crew Exploration Vehicle” means the next generation  
4 spacecraft being planned by the National Aeronautics and Space  
5 Administration.

6 (e) The credit allowed by this section shall not exceed ten  
7 thousand dollars (\$10,000) per year, per qualified employee. For  
8 employees that are qualified employees for part of a taxable year,  
9 the credit shall not exceed ten thousand dollars (\$10,000) multiplied  
10 by a fraction, the numerator of which is the number of months of  
11 the taxable year that the employee is a qualified employee and the  
12 denominator of which is 12.

13 (d) In the case where the credit allowed by this section exceeds  
14 the “tax,” the excess may be carried over to reduce the “tax” in  
15 the following year, and the succeeding years if necessary, until the  
16 credit is exhausted.

17 (e) No credit shall be allowed unless the credit is reflected within  
18 the bid upon which the qualified taxpayer’s contract or subcontract  
19 to manufacture property for ultimate use in a Joint Strike Fighter  
20 or a Crew Exploration Vehicle is based by reducing the amount  
21 of the bid by the amount of the credit allowable.

22 (f) All references to the credit and ultimate cost reductions  
23 incorporated into any successful bid that was awarded a contract  
24 or subcontract and for which a qualified taxpayer is making a claim  
25 shall be made available to the Franchise Tax Board upon request.

26 (g) This section shall remain in effect only until December 1,  
27 2017, and as of that date is repealed.

28 SEC. 11. Section 23637 is added to the Revenue and Taxation  
29 Code, to read:

30 23637. (a) For each taxable year beginning on or after January  
31 1, 2007, and before January 1, 2017, a qualified taxpayer shall be  
32 allowed as a credit against the “tax,” as defined in Section 23036,  
33 an amount equal to 10 percent of the qualified cost of qualified  
34 property that is placed in service in this state.

35 (b) (1) For purposes of this section, “qualified cost” means any  
36 costs that satisfy each of the following conditions:

37 (A) Except as otherwise provided in this subparagraph, is a cost  
38 paid or incurred by the qualified taxpayer for the construction,  
39 reconstruction, or acquisition of qualified property on or after  
40 January 1, 2007, and before January 1, 2017. In the case of any

1 qualified property constructed, reconstructed, or acquired by the  
2 qualified taxpayer (or any person related to the qualified taxpayer  
3 within the meaning of Section 267 or 707 of the Internal Revenue  
4 Code) pursuant to a binding contract in existence on or before  
5 January 1, 2007, costs paid pursuant to that contract shall be subject  
6 to allocation as follows. Contract costs shall be allocated to  
7 qualified property based on a ratio of costs actually paid prior to  
8 January 1, 2007, and total contract costs actually paid. "Cost paid"  
9 shall include, without limitation, contractual deposits and option  
10 payments. To the extent of costs allocated, whether or not currently  
11 deductible or depreciable for tax purposes, to a period prior to  
12 January 1, 2007, the cost shall be deemed allocated to property  
13 acquired before January 1, 2007, and is thus not a "qualified cost."

14 (B) Except for capitalized labor costs as described in  
15 subparagraph (B) of paragraph (1) of subdivision (d), is an amount  
16 upon which the qualified taxpayer has paid, directly or indirectly,  
17 as a separately stated contract amount or as determined from the  
18 records of the qualified taxpayer, sales or use tax under Part 1  
19 (commencing with Section 6001).

20 (C) Is an amount properly chargeable to the capital account of  
21 the qualified taxpayer.

22 (2) (A) For purposes of this subdivision, any contract entered  
23 into on or after January 1, 2007, that is a successor or replacement  
24 contract to a contract that was binding before January 1, 2007,  
25 shall be treated as a binding contract in existence before January  
26 1, 2007.

27 (B) If a successor or replacement contract is entered into on or  
28 after January 1, 2007, and the subject of the successor or  
29 replacement contract relates both to amounts for the construction,  
30 reconstruction, or acquisition of qualified property described in  
31 the original binding contract and to costs for the construction,  
32 reconstruction, or acquisition of qualified property not described  
33 in the original binding contract, then the portion of those amounts  
34 described in the successor or replacement contract that were not  
35 described in the original binding contract shall not be treated as  
36 costs paid or incurred pursuant to a binding contract in existence  
37 on or prior to January 1, 2007, under subparagraph (A) of paragraph  
38 (1).

39 (3) (A) For purposes of this section, an option contract in  
40 existence before January 1, 2007, under which a qualified taxpayer,

or any other person related to the qualified taxpayer within the meaning of Section 267 or 707 of the Internal Revenue Code, had an option to acquire qualified property, shall be treated as a binding contract under the rules in paragraph (2). For purposes of this subparagraph, an option contract shall not include an option under which the optionholder will forfeit an amount less than 10 percent of the fixed option price in the event the option is not exercised.

(B) For purposes of this section, a contract shall be treated as binding even if the contract is subject to a condition.

(c) (1) For purposes of this section, “qualified taxpayer” means any taxpayer under an initial contract or subcontract to manufacture property for ultimate use in a Joint Strike Fighter or a Crew Exploration Vehicle.

(2) In the case of any passthrough entity, the determination of whether a taxpayer is a qualified taxpayer under this section shall be made at the entity level and any credit under this section or Section 17053.37 shall be allowed to the passthrough entity and passed through to the partners or shareholders in accordance with applicable provisions of Part 10 (commencing with Section 17001) or Part 11 (commencing with Section 23001). For purposes of this paragraph, the term “passthrough entity” means any partnership or “S” corporation.

(3) The Franchise Tax Board may prescribe regulations to carry out the purposes of this section, including any regulations necessary to prevent the avoidance of the effect of this section through splitups, shell corporations, partnerships, tiered ownership structures, sale-leaseback transactions, or otherwise.

(d) (1) For purposes of this section, “qualified property” means property that is described as either of the following:

(A) Tangible personal property that is defined in Section 1245(a)(3)(A) of the Internal Revenue Code for use by a qualified taxpayer primarily in qualified activities to manufacture a product for ultimate use in a Joint Strike Fighter or a Crew Exploration Vehicle.

(B) The value of any capitalized labor costs that are direct costs as defined in Section 263A of the Internal Revenue Code allocable to the construction or modification of property described in subparagraph (A).

(2) Qualified property does not include any of the following:

(A) Furniture.

1     ~~(B) Inventory.~~

2     ~~(C) Equipment used to store finished products that have~~  
3 ~~completed the manufacturing process.~~

4     ~~(D) Any tangible personal property that is used in administration,~~  
5 ~~general management, or marketing.~~

6     ~~(e) For purposes of this section:~~

7     ~~(1) “Crew Exploration Vehicle” means the next generation~~  
8 ~~spacecraft being planned by the National Aeronautics and Space~~  
9 ~~Administration.~~

10    ~~(2) “Fabricating” means to make, build, create, produce, or~~  
11 ~~assemble components or property to work in a new or different~~  
12 ~~manner.~~

13    ~~(3) “Joint Strike Fighter” means the next generation air combat~~  
14 ~~strike aircraft developed and produced under the Joint Strike~~  
15 ~~Fighter program.~~

16    ~~(4) “Joint Strike Fighter program” means the multiservice,~~  
17 ~~multinational project conducted by the United States government~~  
18 ~~to develop and produce the next generation of air combat strike~~  
19 ~~aircraft.~~

20    ~~(5) “Manufacturing” means the activity of converting or~~  
21 ~~conditioning property by changing the form, composition, quality,~~  
22 ~~or character of the property for ultimate use in a Joint Strike Fighter~~  
23 ~~or a Crew Exploration Vehicle. Manufacturing includes any~~  
24 ~~improvements to tangible personal property that result in a greater~~  
25 ~~service life or greater functionality than that of the original~~  
26 ~~property.~~

27    ~~(6) “Primarily” means tangible personal property used 50 percent~~  
28 ~~or more of the time in an activity described in subparagraph (A)~~  
29 ~~of paragraph (1) of subdivision (d).~~

30    ~~(7) “Process” means the period beginning at the point at which~~  
31 ~~any raw materials are received by the qualified taxpayer and~~  
32 ~~introduced into the manufacturing, processing, or fabricating~~  
33 ~~activity of the qualified taxpayer and ending at the point at which~~  
34 ~~the manufacturing, processing, or fabricating activity of the~~  
35 ~~qualified taxpayer has altered tangible personal property to its~~  
36 ~~completed form, including packaging, if required. Raw materials~~  
37 ~~shall be considered to have been introduced into the process when~~  
38 ~~the raw materials are stored on the same premises where the~~  
39 ~~qualified taxpayer’s manufacturing, processing, or fabricating~~  
40 ~~activity is conducted. Raw materials that are stored on premises~~



1 other than where the qualified taxpayer's manufacturing,  
2 processing, or fabricating activity is conducted, shall not be  
3 considered to have been introduced into the manufacturing,  
4 processing, or fabricating process.

5 (8) "Processing" means the physical application of the materials  
6 and labor necessary to modify or change the characteristics of  
7 property.

8 (9) "Qualified activities" means manufacturing, processing, or  
9 fabricating of property, beginning at the point at which any raw  
10 materials are received by the qualified taxpayer and introduced  
11 into the process and ending at the point at which the manufacturing,  
12 processing, or fabricating has altered tangible personal property  
13 to its completed form, including packaging, if required.

14 (f) The credit allowed under subdivision (a) shall apply to  
15 qualified property that is acquired by or subject to lease by a  
16 qualified taxpayer, subject to the following special rules:

17 (1) A lessor of qualified property, irrespective of whether the  
18 lessor is a qualified taxpayer, shall not be allowed the credit  
19 provided under subdivision (a) with respect to any qualified  
20 property leased to another qualified taxpayer.

21 (2) For purposes of paragraphs (2) and (3) of subdivision (b),  
22 "binding contract" includes any lease agreement with respect to  
23 the qualified property.

24 (3) (A) For purposes of determining the qualified cost paid or  
25 incurred by a lessee in any leasing transaction that is not treated  
26 as a sale under Part 1 (commencing with Section 6001) of Division  
27 2, the following rules shall apply:

28 (i) Except as provided by subparagraph (C) of this paragraph,  
29 subparagraphs (A) and (C) of paragraph (1) of subdivision (b) shall  
30 not apply.

31 (ii) Except as provided in subparagraph (B) and clause (iii), the  
32 "qualified cost" upon which the lessee shall compute the credit  
33 provided under this section shall be equal to the original cost to  
34 the lessor, within the meaning of Section 18031, of the qualified  
35 property that is the subject of the lease.

36 (iii) The requirement of subparagraph (B) of paragraph (1) of  
37 subdivision (b) shall be treated as satisfied only if the lessor has  
38 made a timely election under either Section 6094.1 or subdivision  
39 (d) of Section 6244 and has paid sales tax reimbursement or use  
40 tax measured by the purchase price of the qualified property within

1 the meaning of paragraph (5) of subdivision (g) of Section 6006.  
2 For purposes of this subdivision, the amount of original cost to  
3 the lessor which may be taken into account under clause (ii) shall  
4 not exceed the purchase price upon which sales tax reimbursement  
5 or use tax has been paid under the preceding sentence.

6 ~~(B) For purposes of applying subparagraph (A) only, the~~  
7 ~~following special rules shall apply:~~

8 (i) The original cost to the lessor of the qualified property shall  
9 be reduced by the amount of any original cost of that property that  
10 was taken into account by a predecessor lessee in computing the  
11 credit allowable under this section.

12 (ii) ~~Clause (i) shall not apply in any case where the predecessor~~  
13 ~~lessee was required to recapture the credit provided under this~~  
14 ~~section pursuant to the provisions of subdivision (g):~~

15 (iii) ~~For purposes of this section only, in any case where a~~  
16 ~~successor lessor has acquired qualified property from a predecessor~~  
17 ~~lessor in a transaction not treated as a sale under Part 1~~  
18 ~~(commencing with Section 6001) of Division 2, the original cost~~  
19 ~~to the successor lessor of the qualified property shall be reduced~~  
20 ~~by the amount of the original cost of the qualified property that~~  
21 ~~was taken into account by any lessee of the predecessor lessor in~~  
22 ~~computing the credit allowable under this section:~~

23 (C) ~~In determining the original cost of any qualified property~~  
24 ~~under this paragraph, only amounts paid or incurred by the lessor~~  
25 ~~on or after January 1, 2007, and before January 1, 2017, shall be~~  
26 ~~taken into account. In the case of any qualified property~~  
27 ~~constructed, reconstructed, or acquired by a lessor pursuant to a~~  
28 ~~binding contract in existence on or prior to January 1, 2007, the~~  
29 ~~allocation rule specified in subparagraph (A) of paragraph (1) of~~  
30 ~~subdivision (b) shall apply in determining the original cost to the~~  
31 ~~lessor of qualified property:~~

32 (D) ~~Notwithstanding subparagraph (A), in the case of any leasing~~  
33 ~~transaction for which the lessee is allowed the credit under this~~  
34 ~~section and thereafter the lessee, or any party related to the lessee~~  
35 ~~within the meaning of Section 267 or 318 of the Internal Revenue~~  
36 ~~Code, acquires the qualified property from the lessor (or any~~  
37 ~~successor lessor) within one year from the date the qualified~~  
38 ~~property is first used by the lessee under the terms of the lease, the~~  
39 ~~lessee's (or related party's) acquisition of the qualified property~~  
40 ~~from the lessor, or successor lessor, shall be treated as a disposition~~

1 by the lessee of the qualified property that was subject to the lease  
2 under subdivision (g):

3 ~~(4) For purposes of determining the qualified cost paid or~~  
4 ~~incurred by a lessee in any leasing transaction that is treated as a~~  
5 ~~sale under Part 1 (commencing with Section 6001), the following~~  
6 ~~rules shall apply:~~

7 ~~(A) Subparagraph (A) of paragraph (1) of subdivision (b) shall~~  
8 ~~be applied by substituting the term “purchase” for the term~~  
9 ~~“construction, reconstruction, or acquisition.”~~

10 ~~(B) Subparagraph (C) of paragraph (1) of subdivision (b) shall~~  
11 ~~apply:~~

12 ~~(C) The requirement of subparagraph (B) of paragraph (1) of~~  
13 ~~subdivision (b) shall be treated as satisfied at the time that either~~  
14 ~~the lessor or the qualified taxpayer pays sales or use tax under Part~~  
15 ~~1 (commencing with Section 6001).~~

16 ~~(5) (A) In the case of any leasing transaction described in~~  
17 ~~paragraph (3), the lessor shall provide a statement to the lessee~~  
18 ~~specifying the amount of the lessor’s original cost of the qualified~~  
19 ~~property and the amount of that cost upon which a sales or use tax~~  
20 ~~was paid within 45 days after the close of the lessee’s taxable year~~  
21 ~~in which the credit is allowable to the lessee under this section:~~

22 ~~(B) The statement required under subparagraph (A) shall be~~  
23 ~~made available to the Franchise Tax Board upon request:~~

24 ~~(g) No credit shall be allowed if the qualified property is~~  
25 ~~removed from the state, is disposed of to an unrelated party, or is~~  
26 ~~used for any purpose not qualifying for the credit provided in this~~  
27 ~~section in the same taxable year in which the taxpayer first places~~  
28 ~~the qualified property in service in this state. If any qualified~~  
29 ~~property for which a credit is allowed pursuant to this section is~~  
30 ~~thereafter removed from this state, disposed of to an unrelated~~  
31 ~~party, or used for any purpose not qualifying for the credit provided~~  
32 ~~in this section within one year from the date the taxpayer first~~  
33 ~~places the qualified property in service in this state, the amount of~~  
34 ~~the credit allowed by this section for that qualified property shall~~  
35 ~~be recaptured by adding that credit amount to the tax of the~~  
36 ~~qualified taxpayer for the taxable year in which the qualified~~  
37 ~~property is disposed of, removed, or put to an ineligible use:~~

38 ~~(h) In the case where the credit allowed by this section exceeds~~  
39 ~~the “tax,” the excess may be carried over to reduce the “tax” in~~

1 the following year, and the succeeding years if necessary, until the  
2 credit is exhausted.

3 (i) ~~(1) No credit shall be allowed under this section if a credit~~  
4 ~~is claimed under Section 23649 in connection with the same~~  
5 ~~property.~~

6 ~~(2) No credit shall be allowed unless the credit is reflected within~~  
7 ~~the bid upon which the qualified taxpayer's contract or subcontract~~  
8 ~~to manufacture property for ultimate use in a Joint Strike Fighter~~  
9 ~~or a Crew Exploration Vehicle is based by reducing the amount~~  
10 ~~of the bid by the amount of the credit allowable.~~

11 ~~(j) All references to the credit and ultimate cost reductions~~  
12 ~~incorporated into any successful bid that was awarded a contract~~  
13 ~~or subcontract and for which a qualified taxpayer is making a claim~~  
14 ~~shall be made available to the Franchise Tax Board upon request.~~

15 ~~(k) This section shall remain in effect only until January 1, 2017,~~  
16 ~~and as of that date is repealed.~~

17 SEC. 12. ~~Section 23685 is added to the Revenue and Taxation~~  
18 ~~Code, to read:~~

19 23685. (a) ~~(1) For taxable years beginning on or after January~~  
20 ~~1, 2007, subject to the limitation in paragraph (2), there shall be~~  
21 ~~allowed to a qualified taxpayer, as designated by the California~~  
22 ~~Film Commission pursuant to subdivision (h), that makes an~~  
23 ~~irrevocable election pursuant to subdivision (h) to claim the credit~~  
24 ~~authorized by this section, as a credit against the "tax," as defined~~  
25 ~~in Section 23036, an amount equal to 12 percent of the qualified~~  
26 ~~amount. A movie of the week and a miniseries, for which an~~  
27 ~~executed licensing agreement from a network or basic cable entity~~  
28 ~~is provided, shall be entitled to an additional 3 percent of the~~  
29 ~~qualified amount.~~

30 ~~(2) The credit allowed by paragraph (1) shall not exceed the~~  
31 ~~lesser of:~~

32 ~~(A) The amount of the credit allocated to the qualified taxpayer~~  
33 ~~by the California Film Commission based on the initial application.~~

34 ~~(B) The amount of the credit calculated based on actual~~  
35 ~~allowable expenditures on the qualified motion picture.~~

36 ~~(C) Three million dollars (\$3,000,000) per qualified motion~~  
37 ~~picture.~~

38 ~~(b) For purposes of this section:~~

39 ~~(1) "Ancillary product" means any article for sale to the public~~  
40 ~~that contains a portion of, or any element of, the motion picture.~~

1 (2) “Budget” means an estimate of all expenses paid or incurred  
2 during the production period of a motion picture. It shall be the  
3 same budget used by the qualified taxpayer and production  
4 company for all qualified motion picture purposes.

5 (3) “Clip use” means a use of any portion of a motion picture,  
6 other than the qualified motion picture, used in the qualified motion  
7 picture.

8 (4) (A) “Employee fringe benefits” means the amount allowable  
9 as a deduction under this part to the qualified taxpayer involved  
10 in the production of the qualified motion picture for any year during  
11 the production period with respect to any of the following:

12 (i) Employer contributions under any pension, profit-sharing,  
13 annuity, or similar plan.

14 (ii) Employer-provided coverage under any accident or health  
15 plan for employees.

16 (iii) The employer’s cost of life or disability insurance provided  
17 to employees.

18 (B) Any amount treated as wages under clause (i) of  
19 subparagraph (A) of paragraph (21) shall not be taken into account  
20 under this paragraph.

21 (5) “Licensing” means any grant of rights to distribute the  
22 qualified motion picture, in whole or in part.

23 (6) “Movie of the week” and “miniseries” both mean a motion  
24 picture, produced for initial exploitation on television, which  
25 contains a scripted storyline requiring two or more consecutive  
26 hours of programming.

27 (7) “New to California” means a television series that has not  
28 previously engaged in principal photography in this state, other  
29 than for a production that is a pilot or presentation.

30 (8) “New use” means any use of a motion picture in a medium  
31 other than the medium for which it was initially created.

32 (9) (A) “Postproduction” means the final activities in a qualified  
33 motion picture’s production, including editing, foley recording,  
34 automatic dialogue replacement, sound editing, scoring and music  
35 editing, beginning and end credits, negative cutting, negative  
36 processing and duplication, the addition of sound and visual effects,  
37 soundmixing, film to tape transfers, encoding, and color correction.

38 (B) “Postproduction” does not include the manufacture or  
39 shipping of release prints.

1 (10) “Preproduction” means the process of preparation for actual  
2 physical production which begins after a qualified motion picture  
3 has received a firm agreement of financial commitment, or is  
4 greenlit, with, for example, the establishment of a dedicated  
5 production office, the hiring of key crew members, and includes,  
6 but is not limited to, activities that include location scouting and  
7 execution of contracts with vendors of equipment and stage space.

8 (11) “Principal photography” means the phase of production  
9 during which the motion picture is actually shot, as distinguished  
10 from preproduction and postproduction.

11 (12) “Production accountant” means an employee of the  
12 production company whose duties include some or all of the  
13 following activities: oversight of production budgets, cost  
14 reporting, order management, payment of expenses, and the review  
15 of financial reports for accuracy and completeness.

16 (13) “Production company” means a company primarily engaged  
17 in qualified production activities that have been approved by the  
18 California Film Commission.

19 (14) “Production period” means the period of time in which the  
20 preproduction, principal photography, and postproduction occurs  
21 until the qualified motion picture is completed, as described in  
22 clause (v) of subparagraph (C) of paragraph (18).

23 (15) (A) “Qualified amount” means all of the following:

24 (i) The total amount paid or incurred during the production  
25 period for qualified wages with respect to the production of each  
26 qualified motion picture.

27 (ii) The total amount paid or incurred during the production  
28 period for qualified property.

29 (iii) Amounts paid or incurred for qualified wages and qualified  
30 property related to the qualified motion picture for preproduction  
31 costs that include set design and construction, props, wardrobe,  
32 prosthetics, testing, and location scouting that are paid or incurred.  
33 In the case of a television series described in clause (ii) of  
34 subparagraph (C) of paragraph (18), the amounts paid or incurred  
35 for the items described in this subparagraph shall be ratably  
36 allocated among the episodes produced in the first season of  
37 production.

38 (B) Notwithstanding subparagraph (A), the term “qualified  
39 amount” shall not include any qualified wages paid or incurred

1 for services performed nor any qualified property purchased or  
2 leased before January 1, 2007.

3 (16) “Qualified entity” means a personal service corporation as  
4 defined in Section 269A(b)(1) of the Internal Revenue Code, a  
5 payroll services corporation, or any entity receiving qualified wages  
6 with respect to services performed by a qualified individual.

7 (17) (A) “Qualified individual” means any individual who  
8 performs services during the production period in an activity related  
9 to the production of a qualified motion picture.

10 (B) “Qualified individual” shall not include either of the  
11 following:

12 (i) Any individual related to the qualified taxpayer as described  
13 in subparagraph (A), (B), or (C) of Section 51(i)(1) of the Internal  
14 Revenue Code.

15 (ii) Any 5 percent owner, as defined in Section 416(i)(1)(B) of  
16 the Internal Revenue Code, of the qualified taxpayer.

17 (18) (A) “Qualified motion picture” means any motion picture  
18 that is produced, adapted, or altered for exploitation in, on, or  
19 through any medium or by any device, including, but not limited  
20 to, a motion picture produced for exploitation in movie theaters,  
21 through any form of television, videotapes, videocassettes, DVDs, or  
22 any other digital format or on commercial carriers. “Qualified  
23 motion picture” shall also include, but shall not be limited to, all  
24 adapted versions thereof, whether adapted for exploitation in any  
25 language, for any media, or otherwise.

26 (B) (i) “Qualified motion picture” shall not include any motion  
27 picture produced for private noncommercial use, such as weddings  
28 or graduations, made by students as part of any educational course,  
29 or any motion picture produced for industrial purposes.

30 (ii) “Qualified motion picture” shall not include a news program,  
31 current events or public events program, talk show, game show,  
32 sporting event or activity, awards show, telethon or other  
33 production that solicits funds, reality television program, a feature  
34 where 80 percent or more of the content consists of  
35 computer-generated images, clip-based programming if more than  
36 50 percent or the content is comprised of licensed footage,  
37 documentaries, variety programs, daytime dramas, strip shows,  
38 one-half-hour (air time) episodic television shows, or any  
39 production that falls within the recordkeeping requirements of  
40 Section 2257 of Title 18 of the United States Code.

1     ~~(C) To qualify as a “qualified motion picture,” all of the~~  
2     ~~following additional conditions shall be satisfied:~~

3     ~~(i) The qualified motion picture shall be a feature with a~~  
4     ~~minimum budget of three million dollars (\$3,000,000) and a~~  
5     ~~maximum budget of seventy-five million dollars (\$75,000,000);~~  
6     ~~or a movie of the week or miniseries with a minimum budget of~~  
7     ~~five hundred thousand dollars (\$500,000) and a maximum budget~~  
8     ~~of seventy-five million dollars (\$75,000,000).~~

9     ~~(ii) A qualified motion picture shall also include a single episode~~  
10    ~~in a single season, not to exceed 22 episodes per season, of a~~  
11    ~~television series new to California with a minimum budget of five~~  
12    ~~hundred thousand dollars (\$500,000) and a maximum budget of~~  
13    ~~one million eight hundred thousand dollars (\$1,800,000). This~~  
14    ~~clause shall only apply to the first three seasons of a television~~  
15    ~~series that is new to California.~~

16    ~~(iii) The actual expenses totaled at the completion of the~~  
17    ~~qualified motion picture must fall within the fiscal ranges~~  
18    ~~established in clause (i) or (ii) at the time of application to the~~  
19    ~~California Film Commission.~~

20    ~~(iv) At least 75 percent of the total days spent in principal~~  
21    ~~photography of a qualified motion picture occur wholly in~~  
22    ~~California.~~

23    ~~(v) Production of the motion picture is completed within 30~~  
24    ~~months of the date on which the qualified taxpayer’s application~~  
25    ~~was approved by the California Film Commission. For purposes~~  
26    ~~of this section, a qualified motion picture is “completed” when the~~  
27    ~~process of postproduction has been finished, and a final answer~~  
28    ~~print or broadcast delivery air master of the qualified motion picture~~  
29    ~~is produced.~~

30    ~~(vi) Principal photography of the qualified motion picture begins~~  
31    ~~within 180 days of the designation of the taxpayer as a qualified~~  
32    ~~taxpayer by the California Film Commission.~~

33    ~~(D) For the purposes of clauses (i) and (ii) of subparagraph (C)~~  
34    ~~the following additional rules apply:~~

35    ~~(i) In computing the total amounts paid or incurred for the~~  
36    ~~production of a qualified motion picture, all amounts paid or~~  
37    ~~incurred by all persons or entities that share in the costs of the~~  
38    ~~qualified motion picture shall be aggregated.~~



1     (ii) ~~In the case of a television series, described in clause (ii) of~~  
2 ~~subparagraph (C), each episode shall be treated as a separate~~  
3 ~~qualified motion picture.~~

4     (E) ~~For purposes of computing the limitations under this~~  
5 ~~paragraph, “wages” means all amounts described in subparagraph~~  
6 ~~(A) of paragraph (21), provided that these amounts are paid or~~  
7 ~~services performed or rendered within this state.~~

8     (19) (A) ~~“Qualified property” means tangible personal property~~  
9 ~~purchased or leased in California and is used primarily in the~~  
10 ~~production of a qualified motion picture.~~

11     (B) ~~“Qualified property” shall not include a story, script, or~~  
12 ~~scenario to be used for a qualified motion picture, or the literary,~~  
13 ~~dramatic, or musical material upon which the qualified motion~~  
14 ~~picture is based or may be adapted, or any rights related to the~~  
15 ~~foregoing.~~

16     (20) (A) ~~“Qualified taxpayer” means an applicant who has been~~  
17 ~~allocated tax credits by the California Film Commission pursuant~~  
18 ~~to subdivision (h).~~

19     (B) (i) ~~In the case of any passthrough entity, the determination~~  
20 ~~of whether a taxpayer is a qualified taxpayer under this section~~  
21 ~~shall be made at the entity level and any credit under this section~~  
22 ~~is not allowed to the passthrough entity, but shall be passed through~~  
23 ~~to the partners or shareholders in accordance with applicable~~  
24 ~~provisions of Part 10 (commencing with Section 17001) or Part~~  
25 ~~11 (commencing with Section 23001). For purposes of this~~  
26 ~~paragraph, “passthrough entity” means any entity taxed as a~~  
27 ~~partnership or “S” corporation.~~

28     (ii) ~~In the case of an “S” corporation, the credit allowed under~~  
29 ~~this section shall not be used by an “S” corporation as a credit~~  
30 ~~against a tax imposed under Chapter 4.5 (commencing with Section~~  
31 ~~23800) of Part 11 of Division 2.~~

32     (21) (A) ~~“Qualified wages” means all of the following:~~

33     (i) ~~Any wages reported under Section 13050 of the~~  
34 ~~Unemployment Insurance Code that were paid or incurred by the~~  
35 ~~production company involved in the production of a qualified~~  
36 ~~motion picture with respect to a qualified individual for services~~  
37 ~~performed on the qualified motion picture within this state.~~

38     (ii) ~~The portion of any employee fringe benefits paid or incurred~~  
39 ~~by the production company involved in the production of the~~

1 ~~qualified motion picture that are properly allocable to qualified~~  
2 ~~wage amounts described in clause (i):~~

3 ~~(iii) Any payments made to qualified entity for services~~  
4 ~~performed on a qualified motion picture in this state by qualified~~  
5 ~~individuals within the meaning of paragraph (17):~~

6 ~~(iv) Remuneration paid to an independent contractor, as~~  
7 ~~described in Section 2750.5 of the Labor Code, who is a qualified~~  
8 ~~individual for services performed within this state by that qualified~~  
9 ~~individual:~~

10 ~~(B) “Qualified wages” shall not include any of the following:~~

11 ~~(i) Expenses, including wages, for legal or accounting services,~~  
12 ~~except production accountants:~~

13 ~~(ii) Expenses, including wages, in excess of the first twenty-five~~  
14 ~~thousand dollars (\$25,000) paid per person per qualified motion~~  
15 ~~picture for writers, directors, music directors, music composers,~~  
16 ~~music supervisors, producers, and performers, other than~~  
17 ~~background actors with no scripted lines:~~

18 ~~(iii) Expenses, including wages, related to new use, reuse, clip~~  
19 ~~use, licensing, secondary markets, or residual compensation, or~~  
20 ~~the creation of any ancillary product, including, but not limited to,~~  
21 ~~a soundtrack album, toy, game, trailer, or teaser:~~

22 ~~(iv) Expenses, including wages, paid or incurred with respect~~  
23 ~~to acquisition, development, turnaround, or any rights thereto:~~

24 ~~(v) Expenses, including wages, related to financing, overhead,~~  
25 ~~marketing, promotion, or distribution of a qualified motion picture:~~

26 ~~(22) “Residual — compensation” — means — supplemental~~  
27 ~~compensation paid at the time that a motion picture is exhibited~~  
28 ~~through new use, reuse, clip use, or in secondary markets, as~~  
29 ~~distinguished from payments made during production:~~

30 ~~(23) “Reuse” means any use of a qualified motion picture in the~~  
31 ~~same medium for which it was created, following the initial use~~  
32 ~~in that medium:~~

33 ~~(24) “Secondary markets” means media in which a qualified~~  
34 ~~motion picture is exhibited following the initial media in which it~~  
35 ~~is exhibited:~~

36 ~~(e) (1) In the case where the credit allowed under this section~~  
37 ~~exceeds the “tax,” the excess may be carried over to reduce the~~  
38 ~~“tax” in the following year, and succeeding years if necessary,~~  
39 ~~until the credit has been exhausted:~~

1     ~~(2) Notwithstanding Section 23803, the amount of credit claimed~~  
2     ~~by an “S” corporation pursuant to this section shall, be reduced by~~  
3     ~~an amount equal to the amount of credit claimed by the~~  
4     ~~shareholders of the “S” corporation.~~

5     ~~(d) No credit shall be allowed pursuant to this section unless~~  
6     ~~the qualified taxpayer substantiates, by adequate books and records~~  
7     ~~or by sufficient evidence corroborating his or her own statement,~~  
8     ~~that:~~

9     ~~(1) The qualified wages and the qualified property on which~~  
10    ~~the credit was calculated were actually paid or incurred in the~~  
11    ~~amount claimed. Substantiation of this item shall include proof~~  
12    ~~that the services were performed in California and the qualified~~  
13    ~~property was purchased or leased in California.~~

14    ~~(2) The motion picture was a qualified motion picture.~~  
15    ~~Substantiation of this item shall include, but not limited to, the~~  
16    ~~following:~~

17    ~~(A) Identification of each qualified individual.~~

18    ~~(B) The specific start and end dates of production.~~

19    ~~(C) The total wages paid and the amount and type of qualified~~  
20    ~~property purchased.~~

21    ~~(D) The amount of qualified wages paid to each qualified~~  
22    ~~individual.~~

23    ~~(E) Certification from the Director of the California Film~~  
24    ~~Commission that identifies the motion picture as a qualified motion~~  
25    ~~picture.~~

26    ~~(e) The Franchise Tax Board shall provide an annual listing to~~  
27    ~~the State Board of Equalization, in a form and manner agreed upon~~  
28    ~~by the Franchise Tax Board and the State Board of Equalization,~~  
29    ~~of the qualified taxpayers who, during that reporting period, have~~  
30    ~~claimed a credit under this section, including the amount of the~~  
31    ~~credit allowed to each qualified taxpayer.~~

32    ~~(f) Subdivision (e) of Section 19341, relating to interest on~~  
33    ~~overpayments, shall not apply to any return claiming a credit under~~  
34    ~~this section.~~

35    ~~(g) If the qualified taxpayer fails to attach the certification issued~~  
36    ~~by the California Film Commission, in accordance with subdivision~~  
37    ~~(h), the credit shall be disallowed and assessed and collected under~~  
38    ~~Section 19051.~~

39    ~~(h) (1) For purposes of this section, the Director of the~~  
40    ~~California Film Commission shall do all of the following:~~

1     ~~(A) Allocate tax credits to applicants.~~

2     ~~(B) Establish a procedure for qualified taxpayers to file with~~  
3 ~~the California Film Commission a written application, on a form~~  
4 ~~jointly prescribed by the California Film Commission and the~~  
5 ~~Franchise Tax Board, for allocation of tax credits. The application~~  
6 ~~shall be filed under penalty of perjury and include, but not be~~  
7 ~~limited to, the following information:~~

8         ~~(i) The budget for the motion picture production.~~

9         ~~(ii) A one-line shooting schedule.~~

10        ~~(iii) A financing plan for the production.~~

11        ~~(iv) An application fee.~~

12        ~~(v) The copyright registration number for the screenplay, as~~  
13 ~~reflected on the certificate of registration issued under the authority~~  
14 ~~of Section 410 of Title 17 of the United States Code, relating to~~  
15 ~~registration of claim and issuance of certificate.~~

16        ~~(vi) Any other information deemed relevant by the California~~  
17 ~~Film Commission.~~

18     ~~(C) Establish a procedure for qualified taxpayers to make an~~  
19 ~~irrevocable election to claim the tax credit allocation as a credit~~  
20 ~~pursuant to this section or as a credit pursuant to Section 6902.5.~~

21     ~~(D) Determine and designate who is a qualified taxpayer meeting~~  
22 ~~the requirements of this section.~~

23     ~~(E) Process and approve, or reject, all applications on a~~  
24 ~~first-come, first-served basis.~~

25     ~~(F) Provide for the cancellation of the allocated credits if~~  
26 ~~principal photography on the qualified motion picture does not~~  
27 ~~begin within 180 days after notification of the credit allocation by~~  
28 ~~the California Film Commission in accordance with subdivision~~  
29 ~~(i).~~

30     ~~(G) Establish specific audit requirements, in addition to those~~  
31 ~~provided under current law, that must be complied with prior to~~  
32 ~~the issuance of the certificate required by subparagraph (H), and~~  
33 ~~provide for the reallocation of previously approved credits that are~~  
34 ~~disallowed pursuant to the audit requirements, in accordance with~~  
35 ~~subdivision (i).~~

36     ~~(H) Issue a certificate to the qualified taxpayer setting forth the~~  
37 ~~name of the qualified taxpayer, the identification of the qualified~~  
38 ~~motion picture, and the total amount of the tax credit allocated.~~

39     ~~(2) No later than \_\_\_\_\_ 2007, the California Film Commission~~  
40 ~~shall promulgate rules and regulations necessary to establish~~

1 ~~procedures, processes, requirements, and rules identified in or~~  
2 ~~required to implement this section. Rules and regulations may be~~  
3 ~~adopted on an emergency basis if necessary to meet the March 1,~~  
4 ~~2008, deadline. The California Film Commission may amend these~~  
5 ~~rules and regulations as necessary. The California Film~~  
6 ~~Commission may adopt rules and regulations to more narrowly~~  
7 ~~define the terms listed in subdivision (b) to limit their meaning,~~  
8 ~~but may not expand the definition of any terms defined in~~  
9 ~~subdivision (b).~~

10 (i) ~~The aggregate amount of credits that may be allocated in any~~  
11 ~~calendar year pursuant to this section and Section 17053.85 shall~~  
12 ~~be an amount equal to the sum of all of the following:~~

13 (1) ~~Ten million dollars (\$10,000,000) for each calendar quarter,~~  
14 ~~and each calendar quarter thereafter.~~

15 (2) ~~The unused credit ceiling, if any, for the preceding calendar~~  
16 ~~quarter.~~

17 (3) ~~The amount of previously allocated credit canceled or~~  
18 ~~disallowed in the preceding calendar quarter by reason of~~  
19 ~~subparagraph (F) or subparagraph (G) of paragraph (1) of~~  
20 ~~subdivision (h).~~

21 (j) ~~The California Film Commission shall provide a list, at least~~  
22 ~~annually, to the Franchise Tax Board, in the form and manner as~~  
23 ~~shall be determined by the California Film Commission and the~~  
24 ~~Franchise Tax Board, of the names, taxpayer identification~~  
25 ~~numbers, including taxpayer identification numbers of each partner~~  
26 ~~or shareholder, as applicable, the qualified motion pictures for~~  
27 ~~which tax credit was allocated, and the total amount of the tax~~  
28 ~~credit allocated to each qualified taxpayer.~~

29 (k) ~~This section shall remain in effect only until January 1, 2017,~~  
30 ~~and as of that date is repealed, unless a later enacted statute, that~~  
31 ~~is enacted before January 1, 2017, deletes or extends that date.~~

32 SEC. 13. ~~Section 23686 is added to the Revenue and Taxation~~  
33 ~~Code, to read:~~

34 23686. (a) (1) ~~For taxable years beginning on or after January~~  
35 ~~1, 2007, subject to the limitation in paragraph (2), there shall be~~  
36 ~~allowed to a qualified commercial production company, as~~  
37 ~~designated by the California Film Commission pursuant to~~  
38 ~~subdivision (g), as a credit against the "tax," as defined in Section~~  
39 ~~23036, an amount equal to 12 percent of the incremental qualified~~  
40 ~~production costs.~~

~~(2) The credit allowed by paragraph (1) shall not exceed the lesser of:~~

~~(A) Five hundred thousand dollars (\$500,000) per qualified production company per calendar year.~~

~~(B) The amount of the credit allocated by the California Film Commission to the qualified commercial production company pursuant to subdivision (g).~~

~~(b) For the purposes of this section:~~

~~(1) "Base year" is the taxable year preceding the taxable year for which the credit is claimed.~~

~~(2) (A) "Employee fringe benefits" means the amount allowable as a deduction under this part to the qualified commercial production company involved in the production of the qualified commercial for any year during the production period with respect to any of the following:~~

~~(i) Employer contributions under any pension, profit-sharing, annuity, or similar plan.~~

~~(ii) Employer-provided coverage under any accident or health plan for employees.~~

~~(iii) The employer's cost of life or disability insurance provided to employees.~~

~~(B) Any amount treated as wages under clause (i) of subparagraph (A) of paragraph (10) shall not be taken into account under this paragraph.~~

~~(3) "Incremental qualified production costs" are any qualified production costs for the taxable year greater than the qualified production costs for the base year.~~

~~(4) "Principal photography" means the phase of production during which the qualified commercial is actually shot.~~

~~(5) "Postproduction" means the final activities in a qualified commercial's production, including, but not limited to, offline editorial, online editorial, dailies, color correction, compositing, CGI, graphics, sound editorial, sound mixing, sound design, automated dialogue replacement, foley recording, music composition and scoring, and duplication associated with the above process.~~

~~(6) (A) "Qualified commercial" means a commercial or advertisement composed of moving images and sounds that is recorded on film, videotape, or other digital medium, created for display on a network, regional channel, or cable where 75 percent~~

1 of the total production days spent in principal photography occur  
2 wholly in California.

3 (B) ~~“Qualified commercial” shall not include any program length~~  
4 ~~production with an advertising component including a documentary~~  
5 ~~length commercial, an infomercial, news, or current affairs~~  
6 ~~program, interview or talk program, network promotion (short~~  
7 ~~form content intended to promote other programming), sporting~~  
8 ~~event, game show, award ceremony, daytime drama, reality~~  
9 ~~entertainment programming or program intended primarily for~~  
10 ~~industrial, corporate, or institutional end users, fundraising or~~  
11 ~~political commercial, a program consisting primarily of stock~~  
12 ~~footage, a program produced by an organization organized under~~  
13 ~~Section 527 of the Internal Revenue Code, or any production that~~  
14 ~~falls within the recordkeeping requirements of Section 2257 of~~  
15 ~~Title 18 of the United States Code.~~

16 (7) (A) ~~“Qualified commercial production company” means a~~  
17 ~~taxpayer, allocated tax credits by the California Film Commission~~  
18 ~~pursuant to subdivision (g), that is principally engaged in the~~  
19 ~~production of a qualified commercial and has control over the~~  
20 ~~selection of production location, deployment, or management of~~  
21 ~~the production equipment, and directly employs the production~~  
22 ~~crew on the qualified commercial, or is a taxpayer who provides~~  
23 ~~qualified postproduction services.~~

24 (B) (i) ~~In the case of any passthrough entity, the determination~~  
25 ~~of whether a taxpayer is a qualified commercial production~~  
26 ~~company under this section shall be made at the entity level and~~  
27 ~~any credit under this section is not allowed to the passthrough~~  
28 ~~entity, but shall be passed through to the partners or shareholders~~  
29 ~~in accordance with applicable provisions of Part 10 (commencing~~  
30 ~~with Section 17001) or Part 11 (commencing with Section 23001).~~  
31 ~~For the purposes of this paragraph, “passthrough entity” means~~  
32 ~~any entity taxed as a partnership or “S” corporation.~~

33 (ii) ~~In the case of an “S” corporation, the credit allowed under~~  
34 ~~this section shall not be used by an “S” corporation as a credit~~  
35 ~~against a tax imposed under Chapter 4.5 (commencing with Section~~  
36 ~~23800) of Part 11 of Division 2.~~

37 (8) (A) ~~“Qualified individual” means any individual who~~  
38 ~~performs services during the production period in an activity related~~  
39 ~~to the production of a qualified commercial.~~

~~(B) “Qualified individual” shall not include either of the following:~~

~~(i) Any individual related to the qualified commercial production company as described in subparagraph (A), (B), (C), or Section 51(i)(1) of the Internal Revenue Code.~~

~~(ii) Any 5 percent owner, as defined in Section 416(i)(1)(B) of the Internal Revenue Code, of the qualified commercial production company.~~

~~(9) “Qualified production costs” means all of the following:~~

~~(A) Costs for tangible property used and services performed directly and predominately in the production of a qualified commercial.~~

~~(B) Costs for qualified wages, technical and crew production costs, allocable portions of depreciation on equipment directly used in production, rental or other expenditures for commercial production facilities, props, makeup, wardrobe, film processing, camera rental, sound recording, set construction, lighting, on-location meals, and lodging.~~

~~(C) Costs for equipment and services required to complete postproduction of the qualified commercial.~~

~~(D) “Qualified production costs” does not include costs for story, script, or scenario to be used for a qualified commercial, or any qualified wages paid or incurred before January 1, 2007.~~

~~(10) (A) “Qualified wages” means all of the following:~~

~~(i) Any wages reported under Section 13050 of the Unemployment Insurance Code that were paid or incurred by the qualified commercial production company involved in the production of a qualified commercial with respect to a qualified individual for services performed on the qualified commercial production within this state.~~

~~(ii) The portion of any employee fringe benefits paid or incurred by the qualified commercial production company involved in the production of a qualified commercial that are properly allocation to qualified wage amounts described in clause (i).~~

~~(iii) Remuneration paid to a qualified individual for services performed within this state by that qualified individual.~~

~~(iv) Remuneration paid to an independent contractor, as described in Section 2750.5 of the Labor Code, who is a qualified individual for services performed in this state by that qualified individual.~~



1     ~~(B) “Qualified wages” shall not include wages, salaries, or other~~  
2     ~~compensation for writers, directors, music directors, producers~~  
3     ~~and performers (other than background actors with no scripted~~  
4     ~~lines who are employed by a qualified commercial production~~  
5     ~~company.~~

6     ~~(e) (1) In the case where the credit allowed under this section~~  
7     ~~exceeds the “tax,” the excess may be carried over to reduce the~~  
8     ~~“tax” in the following year, and succeeding years if necessary,~~  
9     ~~until the credit has been exhausted.~~

10    ~~(2) Notwithstanding Section 23803, the amount of credit claimed~~  
11    ~~by an “S” corporation pursuant to this section shall be reduced by~~  
12    ~~an amount equal to the amount of credit claimed by the~~  
13    ~~shareholders of the “S” corporation.~~

14    ~~(d) No credit shall be allowed pursuant to this section unless~~  
15    ~~the qualified commercial production company substantiates, by~~  
16    ~~adequate books and records or by sufficient evidence corroborating~~  
17    ~~his or her own statement, that:~~

18    ~~(1) The incremental qualified production costs upon which the~~  
19    ~~credit was calculated were actually paid or incurred in the amount~~  
20    ~~claimed.~~

21    ~~(2) The commercial was a qualified commercial. Substantiation~~  
22    ~~of this item shall include, but is not limited to, the following:~~

23    ~~(A) Identification of each qualified individual.~~

24    ~~(B) The specific start and end dates of production.~~

25    ~~(C) The total wages paid.~~

26    ~~(D) The amount of qualified wages paid to each qualified~~  
27    ~~individual.~~

28    ~~(E) Certification from the Director of the California Film~~  
29    ~~Commission as required in subdivision (g).~~

30    ~~(e) Subdivision (e) of Section 19341, relating to interest on~~  
31    ~~overpayments, shall not apply to any return claiming a credit under~~  
32    ~~this section.~~

33    ~~(f) If the qualified commercial production company fails to~~  
34    ~~attach the certification issued by the California Film Commission,~~  
35    ~~in accordance with subdivision (g), the credit shall be disallowed~~  
36    ~~and assessed under Section 19051.~~

37    ~~(g) (1) For purposes of this section, the Director of the~~  
38    ~~California Film Commission shall do all of the following:~~

39    ~~(A) Allocate tax credits to applicants, including establishing a~~  
40    ~~procedure to allocate tax credits among qualified commercial~~

1 ~~production companies pursuant to paragraph (2) of subdivision~~  
2 ~~(h):~~  
3 ~~(B) Establish a procedure for qualified commercial production~~  
4 ~~companies to file with the commission a written application, on a~~  
5 ~~form jointly prescribed by the commission and the Franchise Tax~~  
6 ~~Board, for allocation of tax credits. The application shall be filed~~  
7 ~~under penalty of perjury and include, but not be limited to, the~~  
8 ~~following information:~~  
9 ~~(i) The qualified production costs for the base year.~~  
10 ~~(ii) The qualified production costs for the taxable year in which~~  
11 ~~the credit is claimed.~~  
12 ~~(iii) An application fee.~~  
13 ~~(iv) Any other information deemed relevant by the commission.~~  
14 ~~(C) Determine and designate who is a qualified commercial~~  
15 ~~production company meeting the requirements of this section.~~  
16 ~~(D) Process and approve, or reject, all applications.~~  
17 ~~(E) Establish specific audit requirements, in addition to those~~  
18 ~~provided under current law that must be complied with prior to~~  
19 ~~the issuance of the certificate required by subparagraph (f), and to~~  
20 ~~provide for the reallocation of previously approved credits that are~~  
21 ~~disallowed pursuant to the audit requirements, in accordance with~~  
22 ~~subdivision (h):~~  
23 ~~(F) Issue a certificate to the qualified taxpayer setting forth the~~  
24 ~~name of the qualified taxpayer and the total amount of the tax~~  
25 ~~credit allocated.~~  
26 ~~(2) No later than \_\_\_\_\_ 2007, the California Film Commission~~  
27 ~~shall promulgate rules and regulations necessary to establish~~  
28 ~~procedures, processes, requirements, and rules identified in or~~  
29 ~~required to implement this section. Rules and regulations may be~~  
30 ~~adopted on an emergency basis if necessary to meet the March 1,~~  
31 ~~2008, deadline. The California Film Commission may amend these~~  
32 ~~rules and regulations as necessary. The California Film~~  
33 ~~Commission may adopt rules and regulations to more narrowly~~  
34 ~~define the terms listed in subdivision (b) to limit their meaning,~~  
35 ~~but may not expand the definition of any terms defined in~~  
36 ~~subdivision (b):~~  
37 ~~(h) (1) The aggregate amount of credits that may be allocated~~  
38 ~~in any calendar year pursuant to this section and Section 17053.86~~  
39 ~~shall be an amount equal to the sum of all of the following:~~

1 (A) Twenty million dollars (\$20,000,000) for the 2008 calendar  
2 year, and each calendar year thereafter.

3 (B) The unused credit ceiling, if any, for the preceding calendar  
4 years.

5 (C) The amount of previously allocated credit cancelled or  
6 disallowed in the calendar year by reason of subparagraph (E) of  
7 paragraph (1) of subdivision (g).

8 (2) If the amount allocable to qualified commercial production  
9 companies exceeds the aggregate amount of credits that may be  
10 allocated in any calendar year, the credits shall be distributed to  
11 qualified commercial production companies as follows:

12 (A) The California Film Commission shall allocate the credits  
13 on a pro rata basis to qualified commercial production companies  
14 for the designated period.

15 (B) The California Film Commission will compute the pro rata  
16 allocation based on submitted applications from all qualified  
17 commercial production companies within 120 days of the  
18 application due date.

19 (i) The California Film Commission shall provide a list, at least  
20 annually, to the Franchise Tax Board, in the form and manner as  
21 shall be determined by the California Film Commission and the  
22 Franchise Tax Board, of the names, taxpayer identification  
23 numbers, including taxpayer identification numbers of each partner  
24 or shareholder, as applicable, the qualified motion pictures for  
25 which tax credit was allocated, and the total amount of the tax  
26 credit allocated to each qualified taxpayer.

27 (j) This section shall remain in effect only until January 1, 2017,  
28 and as of that date is repealed, unless a later enacted statute, that  
29 is enacted before January 1, 2017, deletes or extends that date.

30 SEC. 14. Section 25128 of the Revenue and Taxation Code is  
31 amended to read:

32 25128. (a) Notwithstanding Section 38006, for taxable years  
33 beginning before January 1, 2007, and for taxable years beginning  
34 on or after January 1, 2017, all business income shall be  
35 apportioned to this state by multiplying the business income by a  
36 fraction, the numerator of which is the property factor plus the  
37 payroll factor plus twice the sales factor, and the denominator of  
38 which is four, except as provided in subdivision (b) or (c):

39 (b) If an apportioning trade or business derives more than 50  
40 percent of its "gross business receipts" from conducting one or

1 more qualified business activities, all business income of the  
2 apportioning trade or business shall be apportioned to this state by  
3 multiplying business income by a fraction, the numerator of which  
4 is the property factor plus the payroll factor plus the sales factor,  
5 and the denominator of which is three.

6 (e) For purposes of this section, a “qualified business activity”  
7 means the following:

8 (1) An agricultural business activity.

9 (2) An extractive business activity.

10 (3) A savings and loan activity.

11 (4) A banking or financial business activity.

12 (d) For purposes of this section:

13 (1) “Gross business receipts” means gross receipts described in  
14 subdivision (e) of Section 25120 (other than gross receipts from  
15 sales or other transactions within an apportioning trade or business  
16 between members of a group of corporations whose income and  
17 apportionment factors are required to be included in a combined  
18 report under Section 25101, limited, if applicable, by Section  
19 25110), whether or not the receipts are excluded from the sales  
20 factor by operation of Section 25137.

21 (2) “Agricultural business activity” means activities relating to  
22 any stock, dairy, poultry, fruit, furbearing animal, or truck farm,  
23 plantation, ranch, nursery, or range. “Agricultural business activity”  
24 also includes activities relating to cultivating the soil or raising or  
25 harvesting any agricultural or horticultural commodity, including,  
26 but not limited to, the raising, shearing, feeding, caring for, training,  
27 or management of animals on a farm as well as the handling,  
28 drying, packing, grading, or storing on a farm any agricultural or  
29 horticultural commodity in its unmanufactured state, but only if  
30 the owner, tenant, or operator of the farm regularly produces more  
31 than one-half of the commodity so treated.

32 (3) “Extractive business activity” means activities relating to  
33 the production, refining, or processing of oil, natural gas, or mineral  
34 ore.

35 (4) “Savings and loan activity” means any activities performed  
36 by savings and loan associations or savings banks which have been  
37 chartered by federal or state law.

38 (5) “Banking or financial business activity” means activities  
39 attributable to dealings in money or moneyed capital in substantial  
40 competition with the business of national banks.

1     ~~(6) “Apportioning trade or business” means a distinct trade or~~  
2     ~~business whose business income is required to be apportioned~~  
3     ~~under Sections 25101 and 25120, limited, if applicable, by Section~~  
4     ~~25110, using the same denominator for each of the applicable~~  
5     ~~payroll, property, and sales factors.~~

6     ~~(7) Paragraph (4) of subdivision (c) shall apply only if the~~  
7     ~~Franchise Tax Board adopts the Proposed Multistate Tax~~  
8     ~~Commission Formula for the Uniform Apportionment of Net~~  
9     ~~Income from Financial Institutions, or its substantial equivalent,~~  
10    ~~and shall become operative upon the same operative date as the~~  
11    ~~adopted formula.~~

12    ~~(8) In any case where the income and apportionment factors of~~  
13    ~~two or more savings associations or corporations are required to~~  
14    ~~be included in a combined report under Section 25101, limited, if~~  
15    ~~applicable, by Section 25110, both of the following shall apply:~~

16    ~~(A) The application of the more than 50 percent test of~~  
17    ~~subdivision (b) shall be made with respect to the “gross business~~  
18    ~~receipts” of the entire apportioning trade or business of the group.~~

19    ~~(B) The entire business income of the group shall be apportioned~~  
20    ~~in accordance with either subdivision (a) or (b), as applicable.~~

21    ~~SEC. 15. Section 25128 is added to the Revenue and Taxation~~  
22    ~~Code, to read:~~

23    ~~25128. (a) Notwithstanding Section 38006, for taxable years~~  
24    ~~beginning on or after January 1, 2007, and before January 1, 2017,~~  
25    ~~all business income of an apportioning trade or business shall be~~  
26    ~~apportioned to this state by multiplying the business income by a~~  
27    ~~fraction, the numerator of which is the property factor plus the~~  
28    ~~payroll factor plus twice the sales factor and the denominator of~~  
29    ~~which is four, except as provided in subdivision (b), (c), or (e).~~

30    ~~(b) (1) If an apportioning trade or business is a qualified~~  
31    ~~taxpayer, the qualified taxpayer may elect to have all business~~  
32    ~~income apportioned to this state for taxable years beginning on or~~  
33    ~~after January 1, 2007, and before January 1, 2017, by multiplying~~  
34    ~~the business income by a fraction, the numerator of which is the~~  
35    ~~property factor plus the payroll factor plus four times the sales~~  
36    ~~factor, and the denominator of which is six. The Franchise Tax~~  
37    ~~Board shall prescribe the form and manner for making the election~~  
38    ~~under this paragraph. No election may be made for a taxable year~~  
39    ~~beginning prior to January 1, 2007.~~

~~(2) A qualified taxpayer making the election under this subdivision shall source sales of prewritten software as tangible personal property pursuant to Section 25135, without regard to method of delivery.~~

~~(3) (A) For purposes of this section, “qualified taxpayer” means an apportioning trade or business that derives more than 50 percent of its “gross business receipts” from conducting a business activity, or combination of activities, described in Principal Business Activity Code (PBAC) 312130, 325410, 333200 (to the extent of semiconductor machinery manufacturing only), 334110, 334200, 334410, 339110, 511210, 517000, 512100, 515100, 515210, or 713100 as prescribed by the Internal Revenue Service.~~

~~(B) A taxpayer that does not satisfy the requirements of subparagraph (A) and that derives more than one billion dollars (\$1,000,000,000) of “gross business receipts” from conducting a business activity or combination of activities described in PBAC 312130, 325410, 333200 (to the extent of semiconductor machinery manufacturing only), 334110, 334200, 334410, 339110, 511210, 517000, 512100, 515100, 515210, or 713100 may elect, on a timely filed original return, to be a qualified taxpayer and to multiply business income by a fraction (hereinafter referred to as the “applicable percentage”), the numerator and the denominator of which shall be determined as set forth under paragraph (1) of subdivision (b). The application of the more than one billion dollars (\$1,000,000,000) test shall be made with respect to the combined “gross business receipts” of all members of the apportioning trade or business that are engaged in one or more activities described in this subparagraph.~~

~~The one-time binding election under this subparagraph shall be made by contract with the Franchise Tax Board in the original return. The Franchise Tax Board shall prescribe the form and manner for making the election under this subparagraph. No election may be made for a taxable year beginning prior to January 1, 2007.~~

~~(C) For purposes of subparagraph (B), “qualified taxpayer” includes all members of the apportioning trade or business that are engaged in one or more activities described in subparagraph (B).~~

~~(D) If a qualified taxpayer described in subparagraph (B) is included in a single combined report under Section 25101 or 25110 with one or more taxpayers that are not qualified taxpayers, to~~

1 apportion the business income of the entire combined group, both  
2 of the following shall apply:

3 (i) The numerator of each factor for the qualified taxpayer shall  
4 be the denominator of the factor for the qualified taxpayer  
5 multiplied by the applicable percentage described in subparagraph  
6 (B) for that qualified taxpayer.

7 (ii) The numerators for each of the factors under this  
8 subparagraph shall be added to the numerators of the other  
9 members of the combined group when determining the  
10 apportionment factor that will be used by the combined group.

11 (e) (1) If an apportioning trade or business derives more than  
12 50 percent of its “gross business receipts” from conducting a  
13 business activity, or combination of activities, described in PBAC  
14 211110, 221210, 324110, 324190, 424700, 425120, 447100,  
15 454312, 486000, or 523130 as prescribed by the Internal Revenue  
16 Service, the taxpayer may elect on a timely filed original return to  
17 apportion all business income of the apportioning trade or business  
18 to this state either in the same manner as a qualified taxpayer  
19 pursuant to subdivision (b), or by multiplying business income by  
20 a fraction, the numerator of which is the property factor plus the  
21 payroll factor plus the sales factor and the denominator of which  
22 is three.

23 (2) The one-time binding election under paragraph (1) shall be  
24 made by contract with the Franchise Tax Board in the original  
25 return. The Franchise Tax Board shall prescribe the form and  
26 manner for making the election. No election may be made for a  
27 taxable year beginning prior to January 1, 2007.

28 (d) An election under subdivision (b) or (c) may be terminated  
29 by the taxpayer if either of the following occurs:

30 (1) The taxpayer is acquired directly or indirectly by a  
31 nonelecting entity that alone or together with those affiliates  
32 included in its combined report is larger than the taxpayer as  
33 measured by equity capital.

34 (2) With the permission of the Franchise Tax Board.

35 (e) If an apportioning trade or business derives more than 50  
36 percent of its gross business receipts from conducting one or more  
37 qualified business activities, all business income of the  
38 apportioning trade or business shall be apportioned to this state by  
39 multiplying the business income by a fraction, the numerator of

1 which is the property factor plus the payroll factor plus the sales  
2 factor and the denominator of which is three.

3 For purposes of this subdivision, a “qualified business activity”  
4 means the following:

5 (1) ~~An agricultural business activity.~~

6 (2) ~~A savings and loan activity.~~

7 (3) ~~A banking or financial business activity.~~

8 (f) For purposes of this section, all of the following definitions  
9 apply:

10 (1) (A) “Gross business receipts” means gross receipts described  
11 in subdivision (e) of Section 25120, other than gross receipts from  
12 sales or other transactions within an apportioning trade or business  
13 between members of a group of corporations whose income and  
14 apportionment factors are required to be included in a combined  
15 report under Section 25101, limited, if applicable, by Section  
16 25110, whether or not the receipts are excluded from the sales  
17 factor by operation of Section 25137.

18 (B) “Gross business receipts” does not include sales arising  
19 from a treasury function of the taxpayer’s trade or business, as  
20 defined in subdivision (f) of Section 25120.

21 (2) (A) “Apportioning trade or business” means a distinct trade  
22 or business whose business income is required to be apportioned  
23 under Sections 25101 and 25120, limited, if applicable, by Section  
24 25110, using the same denominator for each of the applicable  
25 payroll, property, and sales factors.

26 (B) In any case where the income and apportionment factors of  
27 two or more savings and loan associations, banks, or corporations  
28 as described in subdivision (b), (c), or (e) are required to be  
29 included in a combined report under Section 25101, limited, if  
30 applicable, by Section 25110, both of the following shall apply:

31 (i) The application of the more than 50-percent test of  
32 subdivision (b), (c), or (e) shall be made with respect to the “gross  
33 business receipts” of the entire apportioning trade or business of  
34 the group.

35 (ii) The entire business income of the group shall be apportioned  
36 in accordance with subdivision (b), (c), or (e), as applicable.

37 (3) “Agricultural business activity” means activities relating to  
38 any stock, dairy, poultry, fruit, furbearing animal, or truck farm;  
39 plantation, ranch, nursery, or range. “Agricultural business activity”  
40 also includes activities relating to cultivating the soil or raising or



1 harvesting any agricultural or horticultural commodity, including,  
2 but not limited to, the raising, shearing, feeding, caring for, training,  
3 or management of animals on a farm as well as the handling,  
4 drying, packing, grading, or storing on a farm any agricultural or  
5 horticultural commodity in its unmanufactured state, but only if  
6 the owner, tenant, or operator of the farm regularly produces more  
7 than one-half of the commodity so treated.

8 (4) “Savings and loan activity” means any activities performed  
9 by savings and loan associations or savings banks that have been  
10 chartered by federal or state law.

11 (5) “Banking or financial business activity” means activities  
12 attributable to dealings in money or moneyed capital in substantial  
13 competition with the business of national banks.

14 (6) “Equity capital” means issued stock of any class, paid-in  
15 capital and retained earnings, or earned surplus, as set forth on the  
16 balance sheet of the taxpayer or the nonelecting entity, for the  
17 immediately preceding year-end accounting period.

18 (7) All references to Principal Business Activity Codes are as  
19 prescribed by the Internal Revenue Service on December 31, 2005.

20 (g) Any change in the apportionment formula caused by this  
21 section is not consideration for granting a change of the  
22 water’s edge election pursuant to Section 25113.

23 (h) If this section or any portion of this section is held invalid,  
24 or the application of this section to any person or circumstance is  
25 held invalid, that invalidity shall not affect other provisions of the  
26 act adding this section, or the provisions of this section that can  
27 be reasonably separated pursuant to Section 23057.

28 (i) This section shall become operative on January 1, 2007, and  
29 shall remain in effect only until January 1, 2017, and as of that  
30 date is repealed unless a later enacted statute, that is enacted on or  
31 before January 1, 2017, deletes or extends that date.

32 SEC. 16. (a) On and after January 1, 2010, the Business,  
33 Transportation and Housing Agency, or an agency designated by  
34 the Business, Transportation and Housing Agency, shall submit  
35 an annual report to the Governor and the Legislature, on or before  
36 March 1 of each year, evaluating the effectiveness of the film  
37 production tax credits provided by Sections 6902.5, 17053.85,  
38 17053.86, 23685, and 23686 of the Revenue and Taxation Code  
39 in stimulating the growth of the film industry within this state. The  
40 report shall include, but shall not be limited to, the following:

1     ~~(1) The aggregate number of motion pictures and commercials~~  
2     ~~produced nationwide, and the number of motion pictures and~~  
3     ~~commercials attributable to California, for the year preceding the~~  
4     ~~implementation of the tax credit compared to the aggregate number~~  
5     ~~of motion pictures and commercials produced nationwide, and the~~  
6     ~~number of motion pictures and commercials attributable to~~  
7     ~~California, for each year following the implementation of the tax~~  
8     ~~credit.~~

9     ~~(2) A survey-based estimate of the number of~~  
10    ~~California-produced motion pictures and commercials that were~~  
11    ~~retained by the state because of the film production tax credit.~~

12    ~~(3) An estimate from the Franchise Tax Board and the State~~  
13    ~~Board of Equalization of the amount of increased tax revenues~~  
14    ~~derived from California-produced motion pictures and commercials~~  
15    ~~retained by the state because of the film production tax credit.~~

16    ~~(4) A comparison of the dollar amounts awarded pursuant to~~  
17    ~~the film production tax credit provided by Sections 6902.5,~~  
18    ~~17053.85, 17053.86, 23685, and 23686 of the Revenue and~~  
19    ~~Taxation Code as compared to the increased revenue estimates~~  
20    ~~provided by the Franchise Tax Board and the State Board of~~  
21    ~~Equalization.~~

22    ~~(5) The total amount of qualified production costs and total~~  
23    ~~production costs.~~

24    ~~(6) The total amount of tax credits issued under Sections 6902.5,~~  
25    ~~17053.85, 17053.86, 23685, and 23686 of the Revenue and~~  
26    ~~Taxation Code.~~

27    ~~(7) The total amount of qualified payroll paid or incurred by~~  
28    ~~qualified taxpayers and qualified commercial production~~  
29    ~~companies.~~

30    ~~(8) An estimated total amount of sales and use taxes paid and~~  
31    ~~the total amount of state and federal employee incomes taxes~~  
32    ~~withheld and paid by qualified taxpayers and qualified commercial~~  
33    ~~production companies who claimed and received a film production~~  
34    ~~tax credit under Section 6902.5, 17053.85, 17053.86, 23685, or~~  
35    ~~23686 of the Revenue and Taxation Code.~~

36    ~~(9) The demographics and geographic distribution of the~~  
37    ~~workforce involved in the production of qualified motion pictures~~  
38    ~~and qualified commercials that received a film production tax~~  
39    ~~credit under Section 6902.5, 17053.85, 17053.86, 23685, or 23686~~

1 of the Revenue and Taxation Code, to the extent this information  
2 is available.

3 ~~(b) The Business, Transportation and Housing Agency may~~  
4 ~~consult with the Employment Development Department, the~~  
5 ~~Franchise Tax Board, the State Board of Equalization, and agencies~~  
6 ~~of local government before completing its report.~~

7 *SEC. 4. Section 25128 of the Revenue and Taxation Code is*  
8 *amended to read:*

9 25128. (a) Notwithstanding Section 38006, all business income  
10 shall be apportioned to this state by multiplying the business  
11 income by a fraction, the numerator of which is the property factor  
12 plus the payroll factor plus twice the sales factor, and the  
13 denominator of which is four, except as provided in subdivision  
14 (b) or (c).

15 (b) (1) If an apportioning trade or business derives more than  
16 50 percent of its “gross business receipts” from conducting one or  
17 more qualified business activities, all business income of the  
18 apportioning trade or business shall be apportioned to this state by  
19 multiplying business income by a fraction, the numerator of which  
20 is the property factor plus the payroll factor plus the sales factor,  
21 and the denominator of which is three.

22 ~~(e)~~  
23 (2) For purposes of this section, a “qualified business activity”  
24 means the following:

25 ~~(1)~~  
26 (A) An agricultural business activity.

27 ~~(2)~~  
28 (B) An extractive business activity.

29 ~~(3)~~  
30 (C) A savings and loan activity.

31 ~~(4)~~  
32 (D) A banking or financial business activity.

33 (c) (1) *Notwithstanding any other provision of law, for taxable*  
34 *years beginning on or after January 1, 2007, a taxpayer that is a*  
35 *member of an apportioning trade or business may, on behalf of*  
36 *the apportioning trade or business or a subgroup thereof, elect to*  
37 *adjust, as provided in paragraph (2), the fraction described in*  
38 *subdivision (a) or (b), as applicable, by utilizing one of the*  
39 *following alternative methods:*

1 (A) (i) In calculating its business income apportioned to this  
2 state, the apportioning trade or business, or a subgroup thereof,  
3 may add an additional sales factor to the numerator of the fraction  
4 described in subdivision (a) or (b), whichever is applicable, and  
5 may increase the denominator of that fraction by one in each  
6 taxable year for each two hundred fifty million dollars  
7 (\$250,000,000) of qualified expenditures made on or after January  
8 1, 2007.

9 (ii) The apportioning trade or business, or a subgroup thereof,  
10 must submit and certify, with each tax return filed with the  
11 Franchise Tax Board, a summary of the qualified expenditures.

12 (B) (i) The apportioning trade or business, or a subgroup  
13 thereof, may adjust the property factor and the payroll factor used  
14 in the fraction described in subdivision (a) or (b), whichever is  
15 applicable, as follows:

16 (I) Property, otherwise includable in the calculations of the  
17 property factor, as defined in Section 25129, shall be excluded  
18 from the numerator of that property factor if it is in excess of the  
19 value of the taxpayer's real and tangible personal property owned  
20 or rented and used in this state in the base year.

21 (II) (ia) The amount of compensation paid by the taxpayer, in  
22 a taxable year that is in excess of the amount of total compensation  
23 paid in this state in the base year and otherwise includable in the  
24 computations of the payroll factor, as defined in Section 25132,  
25 shall be excluded from the numerator of that payroll factor.

26 (ib) For purposes of this section, "compensation in the base  
27 year" does not include extraordinary events such as deferred  
28 compensation payouts or stock option exercises.

29 (ii) The apportioning trade or business, or a subgroup thereof,  
30 must submit and certify, with each tax return filed with the  
31 Franchise Tax Board, a summary of the new investment made in  
32 this state.

33 (2) (A) On or after January 1, 2007, a taxpayer may elect to  
34 adjust the fraction described in subdivision (a) or (b), whichever  
35 is applicable. The election shall be made by attaching a statement  
36 to the original return identifying the apportioning trade or  
37 business, or a subgroup thereof, specifying the method of adjusting  
38 the apportionment factor as described in subdivision (a) or (b),  
39 and designating the member of the apportioning trade or business,

1 *or a subgroup thereof, that will be required to submit and certify*  
2 *the information, as required by paragraph (1).*

3 *(B) The election may be terminated either by the taxpayer, with*  
4 *the permission of the Franchise Tax Board, or by the Franchise*  
5 *Tax Board, if the taxpayer fails to submit a certification signed by*  
6 *an officer, as required by paragraph (1). The election shall remain*  
7 *in effect until terminated.*

8 *(C) This subdivision shall not be construed to terminate the*  
9 *water's-edge election made by a taxpayer pursuant to Section*  
10 *25113, nor shall it be construed to allow any change in, or*  
11 *adjustments to, that election.*

12 *(D) The Franchise Tax Board shall prescribe rules and*  
13 *regulations to implement the provisions of this subdivision.*

14 (d) For purposes of this section:

15 (1) "Gross business receipts" means gross receipts described in  
16 subdivision (e) of Section 25120 (other than gross receipts from  
17 sales or other transactions within an apportioning trade or business  
18 between members of a group of corporations whose income and  
19 apportionment factors are required to be included in a combined  
20 report under Section 25101, limited, if applicable, by Section  
21 25110), whether or not the receipts are excluded from the sales  
22 factor by operation of Section 25137.

23 (2) "Agricultural business activity" means activities relating to  
24 any stock, dairy, poultry, fruit, furbearing animal, or truck farm,  
25 plantation, ranch, nursery, or range. "Agricultural business activity"  
26 also includes activities relating to cultivating the soil or raising or  
27 harvesting any agricultural or horticultural commodity, including,  
28 but not limited to, the raising, shearing, feeding, caring for, training,  
29 or management of animals on a farm as well as the handling,  
30 drying, packing, grading, or storing on a farm any agricultural or  
31 horticultural commodity in its unmanufactured state, but only if  
32 the owner, tenant, or operator of the farm regularly produces more  
33 than one-half of the commodity so treated.

34 (3) "Extractive business activity" means activities relating to  
35 the production, refining, or processing of oil, natural gas, or mineral  
36 ore.

37 (4) "Savings and loan activity" means any activities performed  
38 by savings and loan associations or savings banks which have been  
39 chartered by federal or state law.

1 (5) “Banking or financial business activity” means activities  
2 attributable to dealings in money or moneyed capital in substantial  
3 competition with the business of national banks.

4 (6) “Apportioning trade or business” means a distinct trade or  
5 business whose business income is required to be apportioned  
6 under Sections 25101 and 25120, limited, if applicable, by Section  
7 25110, using the same denominator for each of the applicable  
8 payroll, property, and sales factors.

9 (7) “Base year” means the year immediately preceding the year  
10 of election.

11 (8) “Qualified expenditures” means, in whole or in part, all of  
12 the following expenditures:

13 (A) Capital expenditures for real and tangible personal property  
14 located in this state.

15 (B) Expenses incurred to acquire, develop, or license intellectual  
16 property in this state.

17 (C) Research and development expenses, as defined in Section  
18 174 of the Internal Revenue Code, incurred in this state.

19 (D) Expenses incurred to develop, enhance, or maintain real  
20 property and tangible personal property located in this state.

21 (E) Capitalized rent paid in this state in excess of the prior year.

22 (F) Compensation and benefits paid to employees in this state  
23 in excess of the prior year.

24 (G) Payments to independent contractors and payroll companies  
25 for work performed in this state in excess of the prior year.

26 (H) Training costs incurred in this state.

27 (I) Costs incurred in providing a basic level of health care to  
28 employees in this state, as defined in the Knox-Keene Act, in excess  
29 of the prior year.

30 (J) Expenditures incurred in connection with funding research  
31 at a four-year public or private college or university located in  
32 California.

33 ~~(7) Paragraph (4)~~

34 (9) Subparagraph (C) of paragraph (2) of subdivision ~~(e)~~ (b)  
35 shall apply only if the Franchise Tax Board adopts the Proposed  
36 Multistate Tax Commission Formula for the Uniform  
37 Apportionment of Net Income from Financial Institutions, or its  
38 substantial equivalent, and shall become operative upon the same  
39 operative date as the adopted formula.

40 ~~(8)~~

1 (10) In any case where the income and apportionment factors  
2 of two or more savings associations or corporations are required  
3 to be included in a combined report under Section 25101, limited,  
4 if applicable, by Section 25110, both of the following shall apply:

5 (A) The application of the more than 50 percent test of  
6 subdivision (b) shall be made with respect to the “gross business  
7 receipts” of the entire apportioning trade or business of the group.

8 (B) The entire business income of the group shall be apportioned  
9 in accordance with either subdivision (a) or (b), as applicable.

10 (e) *The provisions of this section are severable. If any provision*  
11 *of this section or its application is held invalid, that invalidity shall*  
12 *not affect other provisions or applications that can be given effect*  
13 *without the invalid provision or application.*

14 (f) *The amendments made to this section by the act adding this*  
15 *subdivision shall apply to taxable years beginning on or after*  
16 *January 1, 2007.*

17 ~~SEC. 17.~~

18 SEC. 5. Any governing body of any county, city, or district  
19 that votes to allow the exemption provided in Section 6357.7 of  
20 the Revenue and Taxation Code shall notify the State Board of  
21 Equalization on or before December 1, 2007.

22 ~~SEC. 18. The provisions of this act are severable. If any~~  
23 ~~provision of this act or its application is held invalid, that invalidity~~  
24 ~~shall not affect other provisions or applications that can be given~~  
25 ~~effect without the invalid provision or application.~~

26 ~~SEC. 19. No reimbursement is required by this act pursuant to~~  
27 ~~Section 6 of Article XIII B of the California Constitution because~~  
28 ~~the only costs that may be incurred by a local agency or school~~  
29 ~~district will be incurred because this act creates a new crime or~~  
30 ~~infraction, eliminates a crime or infraction, or changes the penalty~~  
31 ~~for a crime or infraction, within the meaning of Section 17556 of~~  
32 ~~the Government Code, or changes the definition of a crime within~~  
33 ~~the meaning of Section 6 of Article XIII B of the California~~  
34 ~~Constitution.~~

35 SEC. 6. *It is the intent of the Legislature that Section 4 of this*  
36 *act does not modify the sales factor, as defined in Section 25134*  
37 *of the Revenue and Taxation Code, used in any special*  
38 *apportionment formulas contained in the regulations promulgated*  
39 *by the Franchise Tax Board pursuant to Section 25137 of the*  
40 *Revenue and Taxation Code.*

1     ~~SEC. 20.~~

2     *SEC. 7.* This act provides for a tax levy within the meaning of

3     Article IV of the Constitution and shall go into immediate effect.

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